Modern Business

A SERIES OF TEXTS PREPARED AS PART OF THE MODERN BUSINESS COURSE AND SERVICE OF THE ALEXANDER HAMILTON INSTITUTE

ALEXANDER HAMILTON INSTITUTE
NEW YORK

Modern Business

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INSURANCE

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MODERN BUSINESS

VOLUME 18

ALEXANDER HAMILTON INSTITUTE

NEW YORK

PREFACE

This volume should prove of value to all business men, most of whom are, or will be, owners of real property. To professional dealers in fire insurance and real estate it should also prove valuable. The authors are specialists who have had experience as university teachers, and have learned how to present the essential principles and details of the businesses they describe, in language that the layman can understand. The subjects of Real Estate and Insurance are so closely related that it has seemed best to combine their treatment in one volume.

Mr. Lindner desires to acknowledge his indebtedness to Mr. Philip A. Benson for his valuable help in the revision of the Text on Real Estate.

THE EDITOR.

TABLE OF CONTENTS

PART I

CHAPTER I

MARINE INSURANCE

CHAPTER II

FIRE INSURANCE IN GENERAL

CHAPTER III

FIRE PREMIUM RATE

CHAPTER IV

FIRE INSURANCE POLICY

CHAPTER V

LIFE INSURANCE

CHAPTER VI

MORTALITY AND INVESTMENT EXPERIENCE

CHAPTER VII

BUSINESS METHODS OF LIFE INSURANCE

CHAPTER VIII

CASUALTY INSURANCE

CHAPTER IX

CASUALTY INSURANCE (*Continued*)

CHAPTER X

EMPLOYERS' LIABILITY INSURANCE AND WORKMEN'S COMPENSATION

PART II

REAL ESTATE

CHAPTER I

THE REAL ESTATE BUSINESS AND ITS INTERESTS

CHAPTER II

LIENS

CHAPTER III

TAXES AND ASSESSMENTS

CHAPTER IV

CONTRACTS

CHAPTER V

CONTRACTS—EXCHANGES AND AUCTION SALES

CHAPTER VI

DEEDS

CHAPTER VII

BONDS AND MORTGAGES

CHAPTER VIII

TRANSFERS AND CLOSINGS OF TITLE AND TITLE INSURANCE

CHAPTER IX

LEASES

CHAPTER X

BROKERAGE

PART I

INSURANCE

INSURANCE

CHAPTER I

MARINE INSURANCE

1. *Place and importance.*—The contract of insurance is widely used in the modern business world. Under its terms one party, the insured, pays to a second party, the insurer, a sum of money in consideration of which the insurer agrees to indemnify the insured for any loss that may arise from some contingency stated in the contract. The contract is the policy, the sum paid as consideration, the premium.

The risks which are covered by insurance are at the present time of the most varied character, and the policies written may assume many forms. The chief divisions of insurance are:

Marine
Fire
Life
Casualty

Each has its peculiar characteristics which will engage our attention. Marine insurance is the oldest form of insurance known. It is therefore natural that it should have had considerable influence in shaping the development of other forms of insurance.

These facts entitle it to the first place in any consideration of insurance as a whole.

2. *Beginning of marine insurance.*—In the form of bottomry, marine insurance was practised among the earliest commercial nations. A loan on bottomry was a favorite form of investment among the ancients. It united an investment with a risk, and because of the element of risk involved in a sea voyage a higher rate of return was allowed on this form of bond, even in countries where there were laws against usury. A bottomry bond is nothing more or less than a loan secured by the body of the vessel. Its equivalent in real estate is a mortgage on the property.

In something like its modern form marine insurance is said to have flourished in the Hanseatic League and among the commercial cities on the Mediterranean Sea. It appears to have been introduced into England by the Lombards, but with the growth of shipping passed later into English hands.

The name most distinctly associated with marine insurance in its earliest days is that of Edward Lloyd. His coffee house in London became the meeting place for business men who specialized in marine matters. At this coffee house sales of vessels were conducted regularly and the business of insurance was carried on. So strong had the insurance business become that it continued after Lloyd's death, and resulted in the formation of the famous institution now known as Lloyd's of London.

In the year 1720 two companies were chartered by

the government of England for the purpose of conducting the business of marine insurance. In consideration of certain payments made for the charters, the right to transact such business was denied to other companies. These companies are still in existence, altho they have of course long since lost any monopolistic privileges which they originally had, and must compete with other companies. When the question of granting charters to these companies was under consideration the members of Lloyd's opposed it vigorously, feeling that it would jeopardize the business in which they were engaged. No such result followed. The two companies that were chartered had permission in their charter to do business in other forms of insurance, and they engaged largely in other branches of insurance. In fact, they did only a small part of the marine insurance business. The bulk of it remained, as heretofore, in the hands of the members of Lloyd's, and in the century that elapsed before the abolition of monopoly privileges and the subsequent establishment of other companies to do a marine business in England, Lloyd's built up its great institution, which has remained unassailable down to the present time.

3. *Marine insurance in the United States.*—In the middle of the eighteenth century the Insurance Exchange was established in New York City. It was an institution similar to Lloyd's, when underwriting was carried on by individuals. By the year 1825, however, this form of underwriting had practically

disappeared. In the meantime companies had been formed that rapidly assumed control of the business which remains today in the hands of corporations.

The development and purposes of marine insurance can be best understood if we give an account of how business is done at Lloyd's.

4. *Lloyd's.*—For a long time Lloyd's was an unincorporated society. In 1871 it was incorporated by an act of Parliament. The act of incorporation defines the objects of the organization as follows:

(a) The carrying on of the business of marine insurance by members of the Society.

(b) The protection of the interests of members of the Society in respect to shipping, cargoes and freights.

(c) The collection, publication and diffusion of intelligence and information with respect to shipping.

As a corporation Lloyd's does not transact the business of marine or any other kind of insurance. It performs for its members the functions which the various stock and other exchanges do for their members. It affords certain facilities for the transaction of business between the members, establishes rules for their guidance, and acts as a general source of information.

Any person who wishes to become a member of Lloyd's and engage in marine insurance must deposit £5,000 "caution money," as it is termed. These deposits amount to $17,000,000 at the present time. Marine insurance is the leading business that is transacted by the members, and it is the business over

which Lloyd's probably exercises the greatest supervision; the members, however, are permitted to engage in other forms of insurance. It is stated that almost any kind of a risk may be insured at Lloyd's.

5. *Policy of insurance.*—The earliest known policy written in the English language dates from 1613; we owe its preservation to a lawsuit. This policy shows that in substance and in form the principles of the contract had been worked out very well at that time. There have been alterations in the policy since, but they are comparatively slight.

6. *Definitions of commercial terms.*—When the owner of a ship wishes to employ it in transporting freight for hire, the contract he makes is called a "contract of affreightment." "Freight" is the money earned by means of this contract. Now the shipowner may not carry the goods himself—that is, take charge of the ship during the voyage—but he may hire the ship out to somebody else. The person who hires the ship is called the "charterer," and the contract which is entered into between the owner of the ship and the charterer is called the "charter party."

The "bill of lading" is the form of contract used when goods which do not require the entire vessel are shipped generally for different persons. It is the receipt of the shipowner and the contract of carriage for the goods placed on his ship. This bill of lading can be indorsed; the indorsement transfers the ownership of the goods to the indorsee.

"Demurrage" is a payment made by the consignee

to the transportation company, for delay in unloading the vessel. It is customary for a company to permit the person to whom goods are consigned a certain number of days in which to unload after the vessel's arrival is reported to him. Should the unloading be delayed beyond these days the consignee pays the company for each twenty-four hours' delay, the amount being specified in the contract.

A "bottomry bond" is a bond given when money is borrowed upon the vessel. This represents one of the oldest forms of investment known. Corresponding to the bottomry bond, which in a sense may be said to represent a mortgage on real estate, is the "respondentia bond." This covers a loan on the cargo and corresponds to a chattel mortgage on personal property.

"Salvage" designates everything that is saved. The loss may, of course, be total when a vessel is lost. But such a case is very rare. Even in the famous case of the *Titanic,* which sank in mid-ocean there was a slight salvage in the form of lifeboats and some other small bits of property that were picked up.

7. *Insurable interest.*—The insurer must have some pecuniary interest in the property which will involve him in actual loss in case it is damaged or destroyed. Otherwise he would merely wager on the outcome. In earlier days an insurable interest was not required. However, the practice was outlawed thru the pas-

sage of an act affecting subjects of Great Britain, as early as 1746.

8. *Information secured for the marine underwriters.*—In any problem which involves probabilities both parties are interested in eliminating as far as possible all unknown quantities, so as to reduce the possible loss to the smallest terms. The underwriter seeks to limit his loss, and the insured seeks to lessen his payment.

The third function of Lloyd's, which is set forth as "the collection, publication and diffusion of intelligence and information with respect to shipping," is therefore of the utmost importance in the development of marine insurance.

Edward Lloyd, in the very beginning of his coffee-house days, apparently appreciated the value of securing the earliest and most reliable information about marine events. He established a paper which ran for about one year, and was discontinued in 1696 owing to a disagreement with the government. He re-established it in 1726—thirty years later. With the exception of the *London Gazette,* it is the oldest newspaper in Europe. The original name was *Lloyd's News,* but it is now known as *Lloyd's List.* The information which has been received at Lloyd's up to midnight is published in this paper, which is issued every afternoon. It records not only every disaster or casualty that occurs, but also every movement from port to port of each vessel that is

noted at any station or by a passing ship. Every year many thousands of telegrams are forwarded to Lloyd's from all parts of the world announcing the movement of vessels.

This system of intelligence, was organized with the beginning of Lloyd's, and it is needless to point out that it is absolutely invaluable to the underwriter. Lloyd's is quite proud of the fact that as early as 1739 its information service was so complete that they were able to report to the Admiralty the capture of Porto Bello by Admiral Vernon before the government had received the news from any official source.

Signal stations for the perfection of this service have been established all over the world, and from these stations not only the entrance and departure of vessels is reported, but probably one hundred thousand movements are recorded during a year. The estimate is that not one vessel in ten reaches a port without having been reported at Lloyd's at some period in her passage.

9. *Captain's register and other functions.*—The records of Lloyd's comprise a complete biography of all seamen who attain command of ships. Naturally this includes a great number who never attain to a captain's degree, but who have received their certificates for lesser positions, and who may be promoted in time to captains' positions.

The record of the captain who commands a vessel is as of much value to the marine underwriter as knowledge of the men who propose to borrow money from

a bank is to the banker. The sketch of the captain's life is very complete, and gives the underwriter all the information which he needs for his business.

Lloyd's maintains an office of inquiry. Relatives of seamen, friends of seamen, or those interested in the voyage in any way may obtain from Lloyd's any information that they have in regard to the movement of the vessel.

The inspection of vessels from the time their construction begins till the end of their life was formerly a survey which Lloyd's conducted itself. This has been taken over by a separate corporation, however, and is conducted by them today. Rating a vessel is a factor of prime importance to the underwriter. On being asked to insure a specified amount on a certain vessel he may turn to this register, ascertain when the vessel was built, the material of which constructed, and what her record has been since that time. The rules for construction are exceedingly rigid, and any vessel attaining the highest rating which is granted by the bureau intrusted with this work has complied with very strict specifications.

10. *Risks assumed.*—The marine policy describes in quaint phrases as follows the risks against which indemnity is offered:

> Touching the adventures and perils which the said company is contented to bear, and take upon itself in this voyage, they are of the seas, men-of-war, fires, enemies, pirates, rovers, thieves, jettisons, letters of mart and countermart, reprisals, takings at sea, arrests, restraints and detainments of all kings, princes or people of what nation, condition or

quality soever, barratry of the master and mariners, and all other perils, losses and misfortunes that have or shall come to the hurt, detriment or damage of the said vessel, or any part thereof.

As if the company feared lest otherwise their enumeration of risks might not be complete, they add the all inclusive "and all other perils, losses and misfortunes."

To comprehend the reason for the broad scope of the marine policy one must go back to its origin. Before insurance became a separate business, the merchants had been in the habit of insuring one another in a cooperative manner. The risks against which they insured one another had reached the large proportions shown in the quotation from the policy. It followed, therefore, that if individuals were to engage in the business of insurance, and so relieve the merchant of that part of the risk of his adventure, they must furnish the merchant with the same protection against the large number of risks which had formerly been furnished him thru cooperation with his fellow-merchants. It would not have been possible to establish the business of marine insurance so successfully if it had failed to give the very ample protection demanded by the necessities of commerce in the early days.

11. *War risks.*—Prior to the outbreak of war in 1914 the world had been so long on a peace basis that by means of special agreements added to the policy, the risk of war had been eliminated and insurance

rates much reduced. When the war came there was no experience to guide the marine underwriter in fixing a proper charge to cover the war risk. Since the development of the modern navies there had been no war between two great maritime powers, with large merchant interests on the sea as well as large sea forces to protect their own commerce and prey on that of the other nations.

There were but two solutions for such a problem. One was to do what one nation did—discontinue its merchant service entirely, calling all vessels in to the nearest ports. The other was for the government to come forward and assume the war risk. Plans for doing the latter had been worked out in Great Britain some time previous to the war, and they were put into execution almost immediately after the war broke out. The arrangement involves cooperation between the shipowner and the government. No group of private individuals could afford to run the risk that might be involved in the destruction of ships by the navy of a foreign power. This element or risk must be borne by a larger body than the underwriters represented, and the nation itself was the only body that was large enough to bear it without undue strain.

In the United States the government established a war risk bureau which assumed the war risk hazard for American ships. The bureau has been very successfully conducted, and the experience gained would be useful to the nation in the event of any future war.

Canadian marine underwriters have had a large vol-

ume of business, especially during the course of the European war. The congestion in shipping ports has caused underwriters considerable anxiety at ports of both shipment and discharge. This extra hazard would not be likely to disappear in war times and consideration in rate-making will be given to this factor. Owing to the demand for freight in consequence of expansion of trade and shortage of ships caused by wastage of war, shipowners are not able to give their vessels the overhauling they necessarily require; consequently, underwriters have in war periods to pay claims for damage which under ordinary circumstances they would not have to meet.

12. *Implied warranties.*—There is a tacit agreement between insurer and insured on four points. They do not appear in the policy, but they are as much a part of it as if they did. These are the following:

(a) The element of good faith. This was set forth in the insurance laws of Amsterdam in 1598, in the following language:

> As contracts of insurance are contracts of good faith, wherein no fraud or deceit ought to take place, in case it be found that the insured or insurers, captains, shippers, pilots, or others, use fraud, deceit, or craft, they shall not only forfeit their payments by their deceit and craft, but shall also be liable to the loss and damage occasioned thereby, and be corporally punished, as a terror and example to others; and, if it be found that they have used notorious malversation and great fraud, they shall be punished with death, even as pirates and robbers.

(b) The seaworthiness of the ship.

(c) The supposition that the voyage will be prosecuted without unnecessary delay from port to port.

(d) The understanding that the business engaged in shall be a legal business and shall conform to all the requirements of law as respects credentials or documents.

13. *What is insured.*—The policy may cover the vessel itself, sometimes described as "lost or not lost," the cargo, or the freight, the latter meaning the sum earned for transporting the cargo from one port to another.

The phrase "lost or not lost" may strike one as peculiar, since it implies that insurance may be taken out on property which is not in existence when the contract is made. This may indeed be the fact. There are many cases in which insurance is desired on property when it is at sea and, whether it exists or not, is unknown to the underwriter or to the parties who seek insurance. This provision, therefore, is as old as the business of marine insurance. In other forms of insurance there is nothing analogous to this peculiar provision of the marine policy.

14. *Valuation of property loss.*—The policy may be written in the form known as a "valued policy," which fixes the amount to be paid in case the property is lost. The amount is not subject to a reconsideration unless it is evident that either there has been a mistake, or that so outrageous a valuation has been given as to show fraud upon the face of the transaction.

If the value is not mentioned, it must be proved. The following information is a guide in this matter:

(a) Goods or merchandise—the prime cost (as it is called), to which the shipping expense and the cost of insurance is added.

(b) The ship—the value at the commencement of the voyage, to which there may be added the outfit, the stores and provisions necessary for the voyage, advances which are made to the crew for wages, and the cost of insurance.

(c) The freight—the gross amount of freight due the ship on her arrival at the designated port, plus the cost of insurance.

(d) Any other objects of insurance not embraced in these three divisions, at their value to the insured at the beginning of the voyage, to which there may be added the cost of insurance.

The specific provision for adding the cost of insurance is peculiar to marine insurance.

15. *Risks insured against.*—The following list classifies the risks insured against:

(a) Those embraced in the phrase "perils of the sea," and fire.

(b) Those which result from the actions of those in charge of the voyage, as the master or the crew.

(c) Those which arise from enemies from without, as men-of-war.

(d) "All other perils."

The first group embraces losses due to winds, waves, collision and fire. Such misfortunes arise un-

der unusual circumstances, and the policy does not under any circumstances cover wear and tear due to the ordinary prosecution of the business.

The second group includes jettison and barratry. Jettison relates to circumstances under which portions of the cargo, or all of it for that matter, may be thrown overboard on account of a storm; while barratry has been thus defined:

> Every species of fraud and knavery committed by the master with the intention of benefiting himself at the expense of the owners, and every wilful act on his part of known illegality, gross malversation, or criminal negligence, by whatever motive induced, whereby the owners or the charterers of the ship are damnified.

An illustration of this form of loss is the scuttling of the ship by the master or crew, or some other wilful infliction of loss.

16. *Losses.*—In marine insurance losses fall into four groups:

1. Total loss
2. General average
3. Particular average
4. Salvage

Total losses may be actual or constructive. Actual total loss includes cases in which there is a complete destruction of the property. This may be illustrated by the case of a ship's sailing on a voyage and never being heard of again.

A constructive total loss occurs when the ship is actually in existence and her position known, but the

cost of floating her may be so large as to absorb and more than absorb the value of the ship. This may happen when a vessel runs ashore during an extremely high tide and it is impossible to float her without an expenditure greater than the value of the vessel. The actual physical injury to the vessel in such a case may be very slight, but from a marine insurance point of view the vessel is as much of a total loss as if she were never heard from again after sailing. When there is a constructive total loss, the insured may give to the underwriter notice of abandonment which turns the vessel over to the underwriters and calls on them for full payment of the loss.

There is a constructive total loss whenever the cost of restoring the vessel, plus the cost of repairing the damages, will exceed her value when she is restored. Practically the same rule holds in regard to the cargo and the freight. If the cost of saving either of these is greater than their value, there is a constructive total loss, and the insured has the same right to indemnity as if he had an actual total loss.

17. *General average.*—In marine insurance the damage that may be sustained by the ship, cargo or freight is subject to the application of the principle of average. This principle is not peculiar to marine insurance; it is a method in vogue for distributing the losses of a venture among the different parties interested, whether there is insurance or not. It is centuries older than insurance.

If, for example, a portion of the cargo has to be

sacrificed to save the ship, the loss does not fall exclusively upon the owner of that part of the cargo which has been thrown overboard. It is shared in proportion to their interest, by all who have a stake in the success of the voyage—the owners of the remainder of the cargo, the shipowner and, if the ship has been chartered, the charterer.

The loss may result from the cutting away of the mast of the vessel or from the sacrifice of some other part. On the Pacific coast of South America, for instance, where harbors are scarce, a vessel may put to sea when a gale arises rather than remain near the shore where she is loading or unloading. The storm may arise so suddenly that there is no time to raise the anchor, and the cable may be cut and lost with the anchor. This is a loss under general average, and would be divided among the three interests, just as a more severe loss would be.

When marine insurance came into use it took over the principle of average. It assumed that the property would be insured for its full value, but if it should not be, then the interested party would be liable to contribute toward any loss in addition to the insurance.

18. *Particular average.*—The somewhat contradictory terms, particular average, are used to describe a loss which may happen to an individual interest only when no sacrifice is made for the benefit of all. A vessel may be unfortunate enough to have an anchor and cable washed overboard during a heavy gale. No

sacrifice has been made, and the ship alone is the loser. The accident is a part of the voyage.

Again, a shipper may have his cargo stowed in the very bottom part of the vessel, and owing to a leak his portion of the cargo may be damaged, but no damage to any other part of the cargo may result. This is a particular and individual loss. In the days before insurance was known, the individual, in such a case, was obliged to sustain the loss alone; now, however, he may protect himself by means of insurance.

19. *Salvage.*—The word "salvage" has two meanings. It denotes, on the one hand, a compensation allowed to persons by whose voluntary exertions the vessel, or the cargo or lives on her are protected in case of wreck, capture or other marine adventure. On the other hand, the word also means that which is saved from a wreck or an abandoned vessel. Compensation for saving and the thing which is saved are both called salvage.

20. *How the conditions in the policy are changed.*—While the body of the policy has not been changed for over a century, the same effect has been reached by means of various clauses that have been added from time to time, or of particular clauses that are introduced into a risk.

The cost of insurance may be reduced by a clause which states that the property is "free of particular average." In such case the underwriter is relieved of any liability for damage or partial damage to the property except in the case of total loss and general

average contribution. This condition, expressed by the phrase "free of particular average," is modified in most cases by the words, "unless the vessel be stranded, sunk, burned or in collision."

The common rule in regard to all printed policies, that if a written clause or an additional clause is added it shall take precedence, applies in the case of the marine insurance policy. Thus, the war risk was eliminated by some such agreement as the following:

Warranted by the assured free from claim on account of capture, seizure, detention or destruction by or arising from hostile forces, civil commotions, riots, or by the acts of officers or other persons acting in the name of belligerents, or in pursuing warlike operations whether before or after declaration of war.

Another illustration of the use of a clause for a specific purpose is the following:

Warranted by the assured not to be loaded in excess of her registered tonnage with either lead, marble, stone, coal or iron; and if loading with grain, warranted to be loaded under the inspection of the Surveyor of the Board of Underwriters, and his certificate as to the proper loading and seaworthiness obtained.

21. *Kinds of policies.*—A time policy is one which insures a vessel for a specific time, generally for one year. In Great Britain no policy may be issued for a longer period, but this rule does not apply in the United States.

A voyage policy, as its name implies, is one which insures a vessel from one port to another, as from New York to Marseilles.

A value policy is one which fixes a definite value on the property that is insured, while an open policy is one where the value is to be determined when ascertained.

A floating policy covers vessel or vessels, however propelled, and insures the goods as soon as they are shipped. The details of each shipment, when received by the consignee, are reported to the insurer and the premiums are paid. This last type of policy is especially for the use of importers who order goods a long time in advance of shipment, and who very frequently do not know, before the goods arrive, that they have been sent forward.

22. *Rates.*—In every large marine center there is a board of underwriters that is charged with the general oversight of the business. Many of the rates are made by the board in a cooperative manner. In the present disturbed condition of maritime affairs these boards are holding daily sessions because the information received is frequently of such a nature as to make it advisable to change rates to some part of the world almost daily, if not oftener. Whether or not the rates are followed by all of the companies, they are a valuable guide to the underwriter.

In the summer of 1916 the normal rates from New York City, not including any risk of war, were as follows for a certain day:

England and France	15¢
Portugal	⅓%
Spain	⅜%

Italy	⅜%
Greece	1%
Norway, Sweden and Denmark—not beyond Malmo	½%
Stockholm	⅝%
Archangel	from 5 to 10%
South Africa via Suez	45¢
China and Japan	¾%
Australia	¾%
San Francisco via Panama	45¢
West Coast of South America	½%
Buenos Aires	45¢

The war schedule, or additional, charges in all of these cases would be a very substantial addition to these rates, dependent upon the particular conditions that might apply on the day when the policy was taken out.

23. *Settlement of losses.*—The settlement of losses in marine insurance is a distinct occupation. The persons who settle the losses are known as "average adjusters." The work, which calls for great skill, ranks as a highly developed specialty.

24. *Rates on the St. Lawrence route.*—Marine insurance rates on the St. Lawrence route have been the center of controversy for many years. The typical complaint may be judged by that of the president of the Canadian Manufacturers' Association, in 1916, who then alleged unfair treatment by insurance companies in the matter of rates. He stated that the fact is capable of ample demonstration that Norwegian shipping, thru the system of mutual marine insurance which has been in effect for many years, has cov-

ered all risks, including those of British North American and St. Lawrence trading, with an average premium rate of slightly less than 5 per cent, and that this has prevailed, not for one year or a few years, but over a period of more than a decade.

This rate is approximately one-half that charged a similar type of shipping when engaged in like traffic, by Lloyd's and British marine underwriters on vessels engaged in British North American and St. Lawrence trade.

This difference in the cost of marine hull insurance is practically a profit in itself, and when there is added to it a very great difference in the cost of cargo insurance, as compared with the United States Atlantic ports of Portland, Boston, New York, Philadelphia and Baltimore, these differences run up into large figures. A mutual insurance scheme on lines somewhat similar to that of Norway might be brought about by a marine insurance board or corporation on which would be represented the Canadian government, the shipping federation and a representative of the combined boards of trade of Halifax, St. John, Montreal, Toronto and Winnipeg. The experience of Norway and other countries that have adopted a mutual system of insurance and the rates of premium which experience has shown to be necessary over a period of years, might be taken as a basis for a plan of this character.

One essential would be that all steam vessels engaged in the coasting or foreign trade, built to Lloyd's

British Corporation or Bureau Veritas classification, be eligible for, and compelled to take out, marine insurance to the extent of not less than 75 per cent of the vessel's value—the premium being variable, as regards the age, character and equipment of the ship. All Canadian tonnage could be grouped to, say, three or four scales of classification for insurance purposes —all government vessels engaged in lighthouse, patrol and such services to be included.

On the other hand, the marine underwriters say that the business of the Norwegian clubs is done wholly in the English marine insurance market, and that Canadian marine underwriters therefore are not directly interested in the question. The Canadian Manufacturers' Association has had this question before them for a long time; some years ago a deputation went to England and thrashed the matter out with a committee of Lloyd's, and apparently came back satisfied.

Here is the opinion of Mr. E. W. S. Morren, a marine underwriter interested in the Canadian territory:

> The majority of Canadian shipping out of the St. Lawrence is made by regular line steamers, on which the rate is low even with the additionals charged for British North American waters. The comparison with rates charged by Norwegian clubs is not a fair one, as they write only Norwegian-owned vessels, and rates are based on the underwriting results of each vessel, and they even charge additional premiums for the use of British North American ports during certain parts of

the year. If the Norwegian club rates are so advantageous to shipowners, it would be rather interesting to learn why so few Norwegian vessels trade in the St. Lawrence and British North American waters. It would appear that the only Norwegian vessels trading are those in the coastwise coal trade and the West India trade; only a very few are in the transatlantic trade, and these carry full cargoes of grain.

REVIEW

Distinguish between particular and general average. Part of a cargo is thrown overboard during a storm to save a ship from foundering. Which rule will apply?

A policy of marine insurance is taken out on a ship. The vessel is lost thru the negligence of the master and crew. Is the company liable?

A cargo is shipped from Smyrna to New York by an agent of the buyer. The day after sailing, the ship runs aground and the cargo is damaged. The agent knows of this but does not communicate with the owner. The owner took out insurance. Is the policy good?

What form of policy is suitable for an importer ordering goods some time before shipment?

A policy of marine insurance is taken out on a fishing vessel on a voyage from Plymouth to the Banks and thence back to Plymouth. The vessel runs out of bait and sails to the nearest port, one hundred miles away, for more. On the way a severe storm is encountered and the vessel founders. May or may not the owner recover under his policy? What part of the chapter supports your conclusion?

In what way may losses which give claim to general average arise?

What is demurrage? Salvage? A charter party?

A vessel moored in a harbor is left aground at ebb tide. She is an old vessel and receives serious damage. Would the damage be covered by the standard marine policy?

CHAPTER II

FIRE INSURANCE IN GENERAL

1. *Purpose of fire insurance.*—Fire insurance indemnifies one who may sustain a "direct loss" by reason of fire. If a claim for a loss is to be sustained under the policy it is necessary that there shall be an actual fire, a "glow," as it has been termed in the court reports. Mere smoke of itself, with no fire, is not sufficient. The phrase "direct loss," with reference to a fire, however small, is used to indicate the damage caused by the smoke of the fire, as well as incidental damage that may be done, as by the use of water in putting it out.

2. *Origin of fire insurance.*—The fire insurance business was carried on in a crude way on the mutual principle previous to 1667, but there was apparently no well-developed system. Moreover, among the guilds there had been for centuries some allowance made for protection against fire losses. If a member suffered loss from fire, his fellow-members made good a portion tho not all of his loss. But the beginning of fire insurance on a commercial basis dates from the year 1667, after the great fire of London.

3. *Nicholas Barbon and Richard Povey.*—Nicholas Barbon of London, a man of considerable education, who had studied medicine, returning from the conti-

nent shortly after the great fire of London, devoted himself to building houses. In conjunction with this, and probably also to further his building plan (altho the facts are not known), he set up an office where he might carry on a business of insuring property against loss by fire. Barbon insured buildings only. These he grouped in two classes—the wooden and the brick or stone.

Richard Povey followed Barbon in the insurance field. His contribution to the business of fire insurance was the insurance of personal property. These two men, then, are properly associated as the founders, so far as the English speaking world is concerned, of the business of protecting real and personal property from loss by fire, which has grown now to such enormous proportions.

4. *Stock companies.*—Insurance companies originated in England in 1720. Previous to that time the business of underwriting had been entirely a matter of individuals or groups of individuals. After 1720 the companies began to branch out into the colonies, and the English companies stand very distinctively for a world-wide business. The business in England is controlled by only a few companies whose capital stock is usually divided into shares of very small amounts, five pounds not being uncommon.

5. *Early American companies.*—On the American continent insurance was practised in the colonies along much the same lines as in England. Groups of individuals combined and underwrote certain properties.

Owing to the scantiness of the population and of the financial resources, the business was one of small proportions until the beginning of the nineteenth century.

The first company was a mutual company in Charleston, S. C., which organized in 1735. It did not survive the great fire of 1740. The next, and a very successful one, was the Philadelphia Contributionship in 1752. Among its first members, and the second man to sign the deed of settlement, was Benjamin Franklin. The real projector of the enterprise was John Smith, whose descendants have been identified with the company ever since.

The third company, also organized in Philadelphia, is mentioned simply because it illustrates a principle. The first company passed a resolution that to facilitate the control of fires all shade trees in front of members' houses must be cut down six months from that date. Members who demurred withdrew and established a mutual insurance company, which they called the Green Tree Company. This company divided its risks into two classes, charging a higher rate when there were shade trees in front of the house.

6. *Early characteristics.*—Fire insurance was local in character from its beginning until about the time of the Civil War. There were many companies, most of them with small capital and limited assets, doing business within a restricted sphere. This feature proved very disastrous to the Illinois, Massachusetts and New York companies when the big conflagrations occurred in Chicago, Boston and New York. The

New York fires, however, occurred in 1835 and 1845, and their effect had passed away when the great fire of Chicago took place in 1871, and the Boston fire in 1872.

7. *Insurable interest.*—In the early days of the business a spirit of gambling, which perhaps was born with it, grew strong. This was not checked until a law was passed decreeing that policies could not be taken out except by those who had an insurable interest in the property. If one wonders that anything else ever could have been the case, it must be remembered that insurance was looked upon as such a visionary project in those days that it was considered much the same as gambling—that is, the risk, or the hazard, in the business was considered in much the same way. The English statute on the subject, which is the basis of all others was that of 14 Geo. III. C. 48. In its recital of the evils arising from gambling contracts it is similar to the statute of 19 Geo. II., applicable to marine insurance, to which reference was made in the preceding chapter (Section 7). The statute of 14 Geo. III. parallels the earlier one, except that it requires an insurable interest in the life or events upon which the policy is taken out, and does not refer to marine insurance at all.

8. *Insurable interest appears in many forms.*—When there is absolute ownership of the property, with no other interest involved, there is no question as to who possesses an insurance interest. The property may be mortgaged and yet the owner may still

have a complete insurable interest in it. The mortgage also possesses an insurable interest. It is only necessary that one have some financial interest in the property. It may be very slight, as a contract for the purchase of the piece of property.

Insurable interest also arises from one's legal relation to, or obligation on account of, the property. The administrator of an estate is charged with the proper care of the property. One of his duties is to safeguard it from loss by fire. If he should fail to take out insurance, and the property should burn and the heirs sustain a loss, he could be held in damages for neglect, and since he can be so held he acquires an insurable interest.

9. *Insurance methods.*—There are four different types of companies that conduct the insurance business today:

(a) The stock companies, which do 95 per cent of the business.

(b) The mutuals. These may be divided into two classes: The first, the small local mutuals which may operate to advantage with a limited line of risks and in a limited territory. They have not succeeded where they have branched out to any great extent. Second, the mill mutuals, as they are called, which specialize in large manufacturing plants. They have had a most successful career. They are primarily organizations for fire prevention, and deal largely with sprinkler risks. These companies have attained a high standard in the work of fire prevention.

(c) Reciprocal underwriters. Insurance business is sometimes carried on by a group of individuals who agree to insure one another. The work is conducted by one person who is appointed as attorney and who transacts the business for the underwriters. He is paid a certain percentage, and out of this he pays the expenses.

(d) Lloyd's. A somewhat freer form of individual business called "Lloyd's" has almost entirely passed away. It is still possible in some parts of the United States for groups of individuals to undertake the business of fire insurance if they do it within certain limits. Many of these organizations spring up, and take the name of Lloyd's because the name is synonymous with insurance.

10. *Extent of insurance.*—The capital of the stock companies in the United States amounts now to about eighty million dollars. The foreign companies—whose home offices or places of incorporation are in some other country—treat the business done in the United States merely as a part of their total business. In a sense, they have no actual capital, so far as this country is concerned, altho at the present time it is considered that they should have in this country not less than the minimum capital required of an American company. As a matter of fact, they have many times that. But in speaking of capital the foreign companies are not considered.

The number of companies engaged in the business is 175. The amount of business written, that is, the

risks for which policies are issued, amounts to forty billions of dollars. The premiums received in the United States represent three hundred and twenty-five million dollars; the losses thru a series of years will average about 55 per cent of the premiums received. Of the remaining 45 per cent the acquisition cost, which covers many services performed by the broker and his commissions, is about 22 per cent. The other expenses of the company will eat up 18 per cent, leaving thru a series of years only about 5 per cent as an underwriting profit. The average rate of premium is now $1.04. This is slightly over 1 per cent for each $100 of business written. The dividends will average for all the companies about 10 per cent. There is, of course, the greatest variation in the dividends, as in other corporations, but this is a fair average.

11. *Working organization.*—In its general features an insurance company does not differ from any other corporation. The chief officer is usually a president, and a foreign company doing business in this country has a resident manager here. There are vice-presidents, secretaries and treasurers. The officer of primary importance is the one in whom is vested the control of the underwriting. The corporation is in the business of selling policies. To sell its policies it must assume risks. The one who determines the lines along which the risks are to be assumed is the underwriter. He may or may not be the president. He may or may not be the one who takes the chief care of the investment features—but he is the one upon

whom the success of the company will ultimately depend. In due order, after the executive officers, there will come the adjusters, the inspectors and the special agents. The latter cover a certain territory, which may be a part of a state, a whole state or several states, according to the business done. They keep in touch with the local situation and aid the local agent.

12. *Local agents.*—The business of fire insurance is transacted largely thru agents. There are thousands of agents; some companies have as many as ten thousand. The business, it must be remembered, is a retail business, not wholesale, and so the large number of salesmen, as they might be called, are necessary. The agent performs, of course, many services for the insured, but he is the "business-getter" for the company in his locality. He is the one whom the insured is most likely to know, since the insured will very seldom come in contact with any of the officers of the company or even with the special agent.

13. *The broker.*—Between the agent and the company has arisen a class of brokers who represent specifically the interest of the insured. They are more numerous in New York City than in any other part of the country, and are found only to a limited extent in the smaller towns. In New York City, for instance, the insured is far more apt to know the broker whom he employs than to know the company.

14. *How the business is transacted.*—We shall have little difficulty in understanding how a fire insur-

ance transaction is effected if we consider in their regular order the six steps involved:

(a) Application for insurance
(b) Inspection of the risk
(c) Making of the rate
(d) Writing of the policy
(e) Collection of the premium
(f) Settlement of the loss

15. *Application.*—A contract of insurance may be terminated at any moment after it has gone into effect. Hence an oral acceptance makes a good contract of insurance. In many of the smaller towns a large amount of the business is applied for and accepted in this way, and the policy goes on in due course. This method, however, would not do for the large centers; in such cities a contract called a binder is used.

It is necessary only to remark that a contract is limited to fifteen days, but that it is a very sound and simple form of contract.

NAME .....
Location .....
on .....
.....
.....

Address of Mortgagee-Payee or of representative thereof.....
.....
Amount $..... Rate *..... Time.....Months

Each of the undersigned companies, for itself only, insures the property above described for the amount set opposite name until the issue of its Standard Policy on the same in place hereof, or until twelve

o'clock noon of the next business day after the risk is declined, by notice to the insured or to the representative of the insured placing the risk; provided, however, that if the address of a mortgagee-payee or of a representative thereof is given above, such notice must also be sent to that address in order to terminate the insurance as to such mortgagee-payee. But in no event shall this insurance be in force over fifteen days from the date of commencement of liability hereunder.

If the policy is already in existence and it is necessary to change it without writing a new policy, there is issued what is called the indorsement agreement, which reads as follows:

Binder Signed	Company	Amount	Date of Commencement of Liability	Signature

Assured .....

Date and Wording of Indorsement: ....., 19

.....

.....

.....

.....

Address of Mortgagee-Payee or of representative thereof.....

.....

Each of the undersigned companies, for itself only, agrees to make the foregoing indorsement on its policy or policies designated below, provided said policy or policies shall be presented for that purpose within fifteen (15) days from the date of its signature hereto, otherwise this agreement to be null and void; and this agreement at any time prior to the making of said indorsement will terminate at twelve o'clock noon on the next business day after notice of such termination to the insured or to the representative of the insured requesting the indorsement; provided, however, that if the address of a mortgagee-payee or of a representative thereof is given above, such notice must also be sent to that address in order to terminate this undertaking as to such mortgagee-payee.

Company	Policy No.	Date Binder Signed	Signature	Date Policy Received	Signature

* Subject to conditions of the $\left\{\begin{matrix}80\\90\\100\end{matrix}\right\}$ % Average Clause.

The making compulsory of signed applications by the would-be insured has been frequently recommended by those interested in the fire-prevention movement. Mr. J. Grove Smith, of the Canadian Commission of Conservation, has suggested legislation invalidating any policy or contract of insurance when issued without the written signed application of the insured or his or their duly appointed agent. It is generally considered reasonable that there should be an authentic declaration of the values to be insured. The fire insurance contract is one of good faith and as one of the parties to the contract gives a written agreement as a matter of course, there is no reason why the other party should not do likewise. The enforcement of written application would act as a deterrent to any who are criminally inclined. The onus of having signed applications, however, rests with the companies.

Whether a general agreement in Canada among the companies in regard to signed applications will be secured, time and competition will decide.

16. *Inspection.*—The insurance company will examine the property that is offered for insurance. What does this inspection mean? Whatever the details, the following points will always be taken into consideration. The general conditions from a civic point of view, in a town or city in which the risk is located, will be considered. These will include not merely the fire department and those related directly to it, such as water supply, or those related directly

to the business of insurance, but many things which perhaps are not ordinarily thought of, such as the kind of streets, police force, high winds and numerous other points. When this foundation has been laid, the individual risk will be considered—its construction, occupancy, hazards, exposure—that is, its relation to the surrounding properties, its fire prevention devices, the general tone of the management, usually called housekeeping. Just as there are no two human beings alike, so in all probability there are no two risks that are absolutely identical.

17. *Details of inspection.*—In the case of the individual risk, some of the points that are noted are as follows: The kind of building, as frame, ordinary, or fireproof; height; area; roof; thickness of floors, floor openings such as stairways, elevators, dumbwaiters and protection, if any. The business conducted, floor by floor, including the nature of the property on each floor; any work that is done, the number of hands employed in the work and the kind of machines used.

The majority of fires in the United States are due to carelessness. Therefore, the inspector goes very carefully into the question of unsafe heating or lighting apparatus, untidiness, broken floors, windows, oily floors and other points which denote a somewhat substandard conception of housekeeping. Fire-fighting devices will be carefully scanned such as the fire pails, the extinguishers, stand pipes, sprinkler system and anything of that nature on the premises. The care of

packing material and kind of doors which separate one building from another will be taken into consideration. When the insurance inspector is thru with the property he probably knows many things about it which the insured himself never suspected and in fact may never have had time to investigate.

18. *Canadian inspection system.*—The Underwriters' Associations in Canada are doing excellent work in regard to inspection. This is described by Mr. A. W. Ross, formerly secretary of the Mainland Board of Fire Underwriters, in the following words:

We maintain a number of experts who have had extensive experience in inspections and applying schedules to various classes of risks. Uniform practices in the manner of conducting the business are demanded, concurrent forms of policies upon all important individual risks are maintained. In this connection, all daily reports are examined, and approved, or otherwise, as the cases may warrant. In the congested or mercantile sections of a city, special inspections and rates are made, each risk being rated upon its own merits. The same thing applies with respect to special hazards and all important risks. The inspections or surveys of each risk, together with detailed information, are kept on file in our offices, and are open to the inspection of all parties interested. It has been the practice of this association to invite the inspection and criticism of the owners of the risks, and we are only too pleased upon every occasion to have the interested parties visit our offices and consult upon any real or supposed grievance which may exist. We advise always to undertake improvements which they may suggest. In this way we can materially improve the hazard in the risk, thereby reducing the rate. In a few instances, we experience some difficulty in inducing owners to undertake suggested improvements, but we find the num-

ber of such persons is gradually becoming less, and our experience proves that the large property owners and public generally are daily becoming more disposed to consult with us on the question of construction and protection than they ever have been before.

Our surveying staff make periodical inspections of the more important risks in so far as it is possible with the assistance employed. Investigations are constantly being made as to the extent and efficiency of fire departments, water supply, character of streets, conditions and construction of buildings in various cities and other important matters incident to the prevention or suppression of fires and the extent of the conflagration hazard.

We also employ, or have made arrangements with other associations for the use of their sprinkling engineers, and we suggest and assist in the drawing up of plans and specifications for the sprinkler equipments and when installed finally inspect and pass upon the same.

REVIEW

How is reciprocal insurance carried on?

How does it differ from a mutual insurance company?

Name six different risks considered in insuring a property.

What is meant by the term "insurable interest?"

A is ninety years of age and he has twenty children and grandchildren. He owns a house which will descend to B if A dies without issue. Has B an insurable interest in the house?

X is ninety years of age and has one son. X is on his deathbed and incapable of making a will thru incurable lunacy. Has the son an insurable interest in X's house?

CHAPTER III

FIRE PREMIUM RATE

1. *Problem of the rate.*—When fire insurance was first established rate-making must have been largely guesswork. Barbon, who was apparently successful in his insurance adventure, either by good fortune or some clue to the problem of which we do not know, evidently made a rate that secured business and at the same time furnished sufficient funds to conduct it. The offices that were founded somewhat later than Barbon's, have handed down to us copies of the tables showing the rates they charged, but no information as to the data on which they were based. In the beginning, fire insurance rates were not based on the value of the property; the policies were issued, and the rate charged on the rental value of the property. This plan did not last more than a generation and, from that time on, the value of the property has been the basis on which the insurance policies have been issued and the rate determined.

It is evident that the business could not have been in existence a very long time before some fires occurred, and even these may have been few among the insured properties. However, they furnished information on which the underwriter could begin to form a

judgment as to a correct rate. In the United States in 1795, when a mutual company was being organized in Boston, Massachusetts, a very careful search was made into the number of properties that had been destroyed or damaged by fire for some thirty-eight years previous to the organization of the company. Previous to 1800, there is no other record of such search being made.

The experience of the companies showed within about a generation that certain properties or certain kinds of businesses were far more subject to fires than other kinds. A private dwelling, for instance, was not as liable to take fire as a business house, and such facts found expression in different rates for the different classes.

2. *Class rating.*—These classes, which came to be some seven in number, and so continued for a long time, divided properties on the basis of non-hazardous; hazardous; extra hazardous and special. Between these, as between non-hazardous and hazardous, they had half classes so that out of this main group of four they developed the seven classes with varying rates of insurance. The principle of this group-rating system was very simple. In each case there was the rate for the building with about five cents added for each class from the lowest up to the highest. The contents of the non-hazardous class were written at the same rate of insurance as the building, but beginning with the next group, as the half hazardous, an additional charge for the contents was made over and above the

proper charge for the building. This simple system lasted until the middle of the 19th century, with the single exception, that before that time some more minute analyses of certain kinds of properties, such as mills, had been made.

3. *First tariff or schedule.*—This method of more closely analyzing properties offered for insurance originated in England and gave rise to tariffs. The first tariff was adopted in 1843 for the woolen mills. From that time on, various classes of businesses have been taken up and special tariffs adopted for each kind of business.

4. *Rating in the United States.*—The entire practice in the United States strictly followed that developed in England except that the rates were increased as the fires were more numerous. There was the same grouping into seven different classes. This was followed in due course by the adoption of tariffs, or as they became and are now known, schedules. The word tariff never became popular when applied to the rating of property. Indeed, it is probably true that the use of the word tariff in connection with rating matters was the occasion of some of the hostilities to the rate-making methods of fire insurance companies, owing to the fact that the word was so closely allied with political matters.

5. *Minimum rates.*—Rates are minimum and specific. A minimum rate applies to a large group of properties such as dwelling houses where the hazard, or risk, as it may be better understood, is uniform in

its character and does not vary much in extent. Minimum rates apply to groups of properties which the underwriter finds he may safely insure without the expense of a specific inspection and the specific rating. Stores and dwellings, including dwellings above the stores, also come under the minimum rates, provided the stores are occupied by a business of a very mild hazard such as dry-goods, groceries, drugs.

6. *Specific rates.*—A specific rating applies where a business, or some operation in it, deemed to have a risk attached. The underwriter goes to greater expense, exercises more care, and an inspection is made by the rating organization and a rate promulgated. The risk in question may be a property with a dwelling above and a store underneath, but the store may be devoted to the sale of furniture, a kind of stock which furnishes the very best of fuel for a fire, with the result that there is usually a heavy damage. In such a store, too, there are usually oils, paints and varnishes, all highly inflammable.

7. *Schedule rating.*—A property in which there is any risk at all owing either to its business or size, should be subjected to a very close analysis of all its features. This analysis is made by means of a tool called the schedule. What enters into a schedule can be seen from the case of theaters and churches. These properties are erected for certain definite and specific purposes. Both are distinguished by large auditoriums, a condition which greatly facilitates the spread of fire once it has started. Schedules for these

types of properties always take the life-hazard into consideration to some extent, altho primarily the fire underwriter is not charged with responsibility for that feature of a property. Let us take a theater for a closer analysis of this type of risk. The modern theater is divided into three divisions: the stage, including all that part of the theater which is behind the proscénium wall; the auditorium where the audience assembles; the entrance which includes the ticket and general offices, and possibly some other features. After the great Iroquois Theater fire in Chicago, a special study of the design of theaters was made and the effort is now to separate these three parts so that a fire, originating in either the entrance or stage portions, may not be communicated to the auditorium and so endanger the audience. The same would be true in regard to a church property where the activities conducted in connection with parish houses are prominent. Such parish houses are frequently attached to the church building without standard separations. Schedule rating splits the rate into parts instead of providing a flat rate, which was a practice for many years. A schedule may make a uniform rate, but one divided into many parts, charging for this defect and crediting for that superior condition. This system of charges and credits shows the property owner where he has fallen below the standard, and where he has reached it.

8. *Universal mercantile schedule.*—There are two schedules which have been very successful in the at-

tempt to make a uniform method for all properties of a given class. One is the universal mercantile schedule. It was published in complete form in 1893 after it had received the benefit of the criticisms brought forth by some six previous editions. The essential features of the schedule are as follows: (1) The key rate which is based wholly on the general conditions of the town or city. It considers all that is within the jurisdiction of the people themselves, covering everything from the water supply up to the paving of the streets, the police force, etc. This is measured by a certain standard and the key rate is fixed accordingly. (2) The building is then analyzed as to walls, height and area, and these are measured by a standard building. For example, a standard building is not supposed to be more than four stories high, since the fire department cannot fight a fire to advantage above that height, hence a charge is made for the additional stories. Good features, which differentiate the property from ordinary buildings, such as extra heavy beams and timbers, first floor, fireproof, etc., receive credits. (3) The occupancy of the building is then analyzed. The schedule includes a list of occupancies which in the beginning numbered over 1,200. In actual practice it has been expanded by 600 further items. The analysis of the occupancy of the building is divided into two parts. The first embraces two features, the risk or hazard and combustibility, while the second part measures the susceptibility to damage. The stock

may not be a very dangerous or combustible stock, but it may be very susceptible to damage. Millinery, for instance, represents such a stock. It will not of itself start a fire very quickly; but will burn rapidly and, owing to its very light nature, it is highly susceptible to damage from smoke, fire or water. (4) The fire-fighting appliances of the risk are then considered. These include water pails, watchman's service, special alarms and perhaps sprinklers. Certain features of location may be considered, as where a building stands on a corner so that a fire may be fought from two sides. All these points help to constitute a property as a favorable risk. (5) The exposure of a building is the next item taken into consideration. This means the danger of fire from the surrounding property. The next classification includes items which are called faults because they need not exist. They mean unsafe stove pipes or heating conditions, untidiness, improper care of waste cans and all the numerous things which are called in business properties, bad housekeeping. For these the underwriter will make fairly stiff charges. They are placed last in the rate as they can be easily corrected when called to the attention of the interested parties. They can then be taken off without recomputation of the whole rate.

9. *Rate of a non-fireproof brick building.*—The rate is based on the Universal Mercantile Schedule; the building has but one tenant, who is a wholesale dealer in drugs.

Key rate for city	.10
Floors, single	.05
Wood ceiling finish	.07
Wooden side wall finish	.08
Floor openings, stairs only	.075
Skylight, non-standard	.15
Electric lighting	.01
Stoves for heating purposes	.01
Sub-standard chimney	.06
Unprotected metal columns	.10
TOTAL	.705
Charge for hazard	.125
TOTAL	.83
Deduct for fire escapes 2% or	.017
Remainder	.813
Add for exposure	.05
TOTAL	.863
Deduct 15% because insurance equal to 80% of the value is carried	.129
FINAL RATE ON BUILDING	.734
Key rate for contents	.769
Susceptibility charge contents	.563
The stock above and below grade floor	.07
TOTAL	1.402
Deduct for fire escapes 2% or	.028
Remainder	1.374
Add for exposure	.06
TOTAL	1.434

Deduct, because insurance equal to 80% of the value is carried, 7½% or ..... .108

FINAL RATE ON CONTENTS 1.326

It would be possible to make a substantial reduction in the rate of insurance on this property by correcting the skylights, for which a charge of .15 gross is made. This would not be a difficult or expensive thing to do. It should be noticed that the charges which build up the schedule are specific amounts, while the credits are percentages.

10. *Analytical schedule.*—The universal schedule probably owes its completion to the energy and persistence of Mr. F. C. Moore. The analytical schedule is equally indebted to Mr. A. F. Dean. The base rate in this schedule is founded on the town conditions. Towns are divided into some seven classes. No. 1, the highest, is one which has everything the underwriter could desire in the shape of water supply, fire department and civic conditions which favor a low fire record. No. 7, the last, shows a complete absence of these, especially of water supply and fire-fighting force. The schedule from this point on is different from the universal in that it makes all charges as well as credits percentages of this base rate. The theory on which this is founded is that there is a relation between the defective conditions of buildings and the town in which they are situated. For instance, if there is a town which is in grade 7 and in that town there is a building with a defective chimney, the charge

for the defective chimney will be a certain percentage, say ten. Now if the town improves so that it grades in class 3, the charge for the defective chimney will still be ten per cent of the base rate. That is, the same relation will exist between the chimney and the base rate of the town then as that which existed between the chimney and the town in the first instance. This shows the schedule as a system of relations between all the forces which make for good or poor conditions in fire matters. The credits are based on a percentage system.

The charges for occupancy are divided into three parts, ignitibility, combustibility and susceptibility. It carries the analysis of the occupancy to a finer point than the universal schedule in that it does not lump the two first conditions into one charge. The first and second charges are percentages, but the third charge, susceptibility, is a flat fixed charge and is based on the principle that when fire has started, the contents have a certain susceptibility to damage which is not affected by their environment.

The treatment of the exposure is very highly developed, the tables providing for something like eighty different conditions. This schedule has been applied over a great extent of property and probably with more uniformity in its application than any other that has been made. The universal schedule is not copyrighted and so it can be changed. With but few exceptions, it has not been used in its true form, but has been adapted more or less by the local boards. The

analytical schedule, however, is copyrighted and cannot be changed without the consent of the copyright holders. This provision of the copyright is an excellent feature since it has enabled the business of fire insurance to have a fair test of the schedule over a wide extent of territory. It has been used in approximately seventeen states.

As a general rule, conditions governing the conduct of the fire insurance business, and the establishment and maintenance of rates, are on parallel lines in Canada and the United States, but the attitude of the people to insurance rating associations has been much more demonstratively hostile in the United States than in Canada. As a consequence, legislation of one kind or another has been general thruout the United States, and while much of it has been wholesome, some of it has been ill-advised.

11. *Rate-making control in Canada.*—The Ontario legislature early in 1917, had under consideration the matter of the control of rate-making, and of rating organizations. Mr. E. P. Heaton, the fire marshal of Ontario, submitted the following instructive memorandum to the Attorney-General of the province:

1. The business of fire insurance is of such commercial importance that it ranks with banking, railway, express and telegraph service, and public interests demand that the institution should be preserved; that its usefulness should be increased, and that its capacity for efficient public service should be unimpaired.

2. It is in the public interest that stability in rates should be established to the end that unjust and discriminatory

conditions should not be allowed to exist, and equally that adequacy of rate should be maintained for the purpose of securing the solvency of the insurance companies.

3. The determination of just and adequate rates must be based upon two fundamental conditions, namely, first, an accurate statistical record of fire losses in classes and territories; and second, upon inspection and written surveys of properties to be insured.

4. It is practically impossible, because of the enormous cost, for companies, large or small, to prepare their own rates, and rate books, involving, as has been said, statistical information, surveying, inspecting and reporting. Co-operation between them is, therefore, in some degree essential.

5. Legislation should, therefore, assist in the proper regulation of the agencies used for rate-making purposes, and, like all supervisory and restrictive laws, should go no further than is absolutely necessary for the protection of the people.

6. Oppressive legislation, that is, legislation forbidding the association of companies for rate-making purposes, has always failed, and has resulted in demoralized commercial conditions.

7. In the State of Missouri, two years ago, such a law was passed by the legislature, whereupon all fire insurance companies, except those of domestic origin, retired from business and completely demoralized commercial credit. Conditions became so bad that the state executive called into conference bankers, manufacturers, merchants and insurance representatives, with the result that the oppressive legislation was withdrawn and a sane law controlling and regulating the rate-making body was substituted. The insurance companies thereupon returned to the state for active business.

A condition exactly similar is now operating in the State of South Carolina. Sixty-seven insurance companies have withdrawn, and it is manifest that with demoralized commercial credit remedial legislation must be enacted.

The whole matter of an effective, yet wise control of various insurance rate-making bodies is of tremendous importance and requires the most thorough and careful consideration.

The trend of the Ontario inquiry, at the time of the writing, leads one to believe that the investigating commission will suggest to the provincial government that the superintendent of insurance be given power to declare rates to be discriminatory. This opinion is based upon the commission's comments on similar legislation in the United States.

12. *Fire protection.*—Closely wrapped up with the business of fire insurance is fire protection. The business of fire insurance may be said to have invented fire protection. It is quite true that there were such things as fire companies before fire insurance was known, but it is equally true that they were on a very small scale and of very primitive development. When the underwriter began to make allowance thru his schedules for certain forms of fire-fighting devices, it at once stimulated the manufacturer to furnish these appliances. At present, thru the underwriters' laboratories of Chicago, nearly all such devices are subject to a test and only those which have passed the test and whose manufacture is subject to inspection by the laboratory force, are accepted by the underwriters for a reduction in the rate of insurance.

Probably the important position held by the great business of fire protection may be understood better if its financial asset is considered. In the United

States, about $250,000,000 worth of property is annually destroyed by fire. Of this sum of money 60 per cent, or $150,000,000, is subject to a return thru the insurance premium. Many fire losses of course are not covered by insurance. Forest fire losses are complete losses and in many other cases the property is underinsured. While $150,000,000 represent the normal amount paid for fire losses, $100,000,000 is used in various ways for expenses. In other words, we have a sum of not less than $250,000,000 paid for fire insurance premiums. Fire-fighting devices steadily reduce this sum, and if the insured can reduce his premium payment five per cent by installing fire pails, it will be a good investment in most cases. A fire pail is the simplest, the oldest and even today one of the most serviceable fire-fighting tools that we have. One of the most modern is the sprinkler. This is a device which is attached to pipes in the ceiling of the building. One sprinkler head is presumed to protect 100 square feet. In a wet pipe-sprinkler system, there is water in the pipes. The sprinkler is held tight by a special solder which melts at about 160 degrees. This releases the cap and the water flows out of the sprinkler head thus putting the fire out. In a building equipped with sprinklers, 90 per cent of the fires which originate are extinguished with not more than three heads opening. If it were not for the fire protection afforded to properties in the form of sprinklers, large manufacturing plants, stores and loft buildings would not be

possible today. We should be confined to very small units as the danger of conflagration would be so great. Again, the sums paid for fire insurance in the City of New York have not increased in the past ten years, altho the liability which the insurance companies are carrying has increased in that time nearly $1,000,000,000. This increased liability is carried for the same amount of money because of (1) the increase in properties of fireproof construction, and (2) the increase in the properties which are equipped with sprinklers.

In 1883, when the sprinklers were first recognized by the insurance companies, the practice was established and continued, until 1905, of computing the rate of insurance in the usual way and of making a percentage allowance for the sprinkler equipment. At first this was 20; then it increased to 30. In 1905, however, especially designed schedules, based on experience, were introduced for risks with sprinkler equipments. The result has been a steady drop in the rate of insurance on sprinkler properties, until today it is a fairly safe statement that the difference in rate between sprinkled and unsprinkled property is, in most cases, 40 per cent.

13. *Rating organizations.*—The making of the rate of fire insurance is the difficult problem connected with the business. This work is done today almost entirely by organizations which are known as rating organizations. These may cover a single city, as Chicago, New York, Philadelphia, Baltimore, Boston,

Washington. They may cover a state or several states. The area embraced depends largely on the local conditions and the volume of business that is to be handled. The making of this rate in the cooperative way is one of the things which the business of fire insurance finds necessary to its existence, and at the same time it is one of the things which the insured is inclined to view with the utmost suspicion. It exposes the business to the epithet "trust" and similar names.

When the underwriters first organized, the attitude of the states was antagonistic, and laws prohibiting such organizations went on many of the statute books. The underwriter was then obliged to conduct the business of rating as a separate matter thru independent raters and, as they were guided in their work by schedules, the underwriter had at least a clue by which to measure his acceptance. The prohibitive phase has gone. The question and the change in the official viewpoint have been investigated in many states.

REVIEW

What do you understand by minimum rate? By specific rate? Of what advantage is the minimum rate?

How is the key rate under the Universal Mercantile schedule determined?

How are the charges and credits under the Universal Mercantile schedule figured?

What elements affect the rate under the analytic schedule?

What is made the basic rate?

How are devices intended for fire protection tested?

CHAPTER IV

FIRE INSURANCE POLICY

1. *Insurance policy.*—In the year 1873, the State of Massachusetts adopted a standard fire insurance policy. If the companies elected to use it, that fact was duly published and thereafter all their policies in that state were issued under the standard form. Some few years later, the standard policy, which had worked so well in its permissive form, was made mandatory and thereafter no policy of fire insurance could be issued in Massachusetts except under the standard form. On May 1, 1887, a standard policy went into force in the State of New York.

Previously the companies had been permitted to prepare their own policy forms. Inasmuch as most properties were insured not in one company, but in several, some degree of uniformity in policies soon became necessary, and did in fact exist among the companies. But there were sufficient variations to produce a somewhat exasperating effect at times. This led to the compulsory standard policy which no one would be willing to depart from today. The importance of the State of New York as a commercial commonwealth has given a widespread use to its standard policy, altho it is of later date than that of Massachusetts.

The standard policy is lettered from A to F for the first six lines and thereafter in numerical order for convenience of reference. The first six lines read as follows:

In consideration of the stipulations herein mentioned and of $..... premium does insure .....
for the term of ..... from the .....
day of ....., 19.., at noon, to the .....
day of ....., 19.., at noon .....
against all direct loss and damage by fire except as hereinafter provided to an amount not exceeding $..... to the following described property while located and contained as described herein and not elsewhere, namely, etc.

A few points in connection with the opening will be noted: (1) The consideration is not merely the premiums paid but the stipulations which are a part of the policy. (2) The courts have decided that the noon specified is that of local time and not standard time, but in Massachusetts there is a special statute which fixes the time as standard. (3) The insurance is against direct loss and damage by fire. Direct loss and damage means not merely damage from the flame but also from smoke and water. (4) The company desires at all times to have the most definite knowledge concerning the property it insures and the location is of primary importance. Therefore, unless the policy is what is called a floating policy, it will apply only where the property is in a special location.

From the point given the policy is numbered line by line. It is unnecessary to repeat the exact language, as the general tenor will be gathered from the

comments made. The first ten lines set forth briefly the limit of the company's liability which cannot, of course, be more than the face value of the policy, or the actual cash value of the property destroyed by the fire, in case this is less than the face value.

Cash means the nearest approximation that can be arrived at, between the company and the insured, as to the amount of cash that will make the insured whole at the time the loss has occurred. The value of the goods destroyed may have been more at the time of the fire than when they were purchased. The insured is entitled to a settlement at the value at the time of the fire. The value may have been less and if that is the case the settlement must be on this lower value. It is not intended that the insurance policy shall do more than indemnify the insured. It aims to make him whole and to put him in as good a position as he was before the fire occurred, but not in a better one.

2. *Restrictions.*—In a document as rigid as a standard policy, since it is a part of the state law, some provision must be made for insuring certain classes of property which the company may be willing to insure, or for granting certain privileges which the company may be willing to grant, but about which it wishes to have exact knowledge.

Lines 11 to 30 contain provisions making the policy void if certain things are done or exist without the consent of the company. Briefly summarized they are as follows: (1) If there is other insurance; (2) if

the plant is a manufacturing establishment and it is continued in operation later than ten at night; (3) if the hazard is increased without notifying the company; (4) if mechanics are employed more than fifteen days at one time for repairs; (5) if the interest in the property is not sole ownership; (6) if the insured property stands on ground not owned in fee simple by the insured; (7) if the property insured is personal and there be a chattel mortgage; (8) if foreclosure proceedings are commenced and notice of a sale given; (9) if there is a change in the title other than by death of the insured; (10) if the policy is assigned before a loss without notification to the company; (11) if illuminating gas is generated within the property; (12) if benzine or similar oils are allowed on the premises; (13) if the building is vacant or unoccupied for ten days.

Each of the conditions above specified renders the property more hazardous than is contemplated in the usual run of risks. The company may be quite willing to grant the privilege for any or all of these conditions. As a matter of fact many are granted as a pure matter of form; if the insured wishes any of these privileges, it is necessary that the policy contain the proper indorsement.

3. *Non-liability.*—Lines 31 to 35 mention causes such as invasion, insurrection or other circumstances when there is a suspension of the real civic authority from which, if losses occur, the insurance company is not liable. These lines also include the much vexed

problem of loss from explosion. The policy provides that the company shall not be liable for loss by explosion unless there is a fire, and then only for the loss caused by the fire. It is needless to point out the difficulty of separating the two forms of loss.

Lines 36 and 37 make provision that the insurance shall immediately cease if the building fall. The company insures a complete construction and not a mass of rubbish; hence this provision.

4. *Non-insurable items.*—Line 38 gives a list of items such as accounts, bills and currency, which the company may not insure. The difficulty of proving the loss in the case of money will be self-evident. If they could be insured the temptation to have such losses would be possibly too much for human nature. Many of the other items such as accounts and evidences of debt have no real insurable value; they represent a certain legal right to property, a right which exists altho the evidence may be destroyed.

5. *Specific items.*—Lines 39 to 41 take up a set of items which the company may insure but which must be mentioned specifically—awnings, patterns, curios and things of that character. In the case of patterns, there is the susceptibility to damage coupled with the fact that in many cases they may represent a value utterly disproportionate to the rest of the plant, as in the case of an iron foundry. The common practice in connection with patterns is to limit the insurance to not more than ten per cent of the face value of the policy. This is probably not a necessary procedure

where the property is insured for its full value or eighty per cent of its value.

The latter part of lines 41 to 44 provides that no loss shall be paid by the company if the property is damaged or the loss increased thru a city ordinance. In some cases, where a city ordinance forbids the erection of a frame building in a certain section of the city, so that when a frame building is destroyed or damaged by fire it may not be rebuilt in the same territory, provision is made for this form of loss, but it is questionable whether it is a loss that is properly insurable under a fire policy. If the insured is obliged to erect a building of better character than the one he lost, then he has the value in the better building. In other words, it is not a loss that he has suffered.

6. *Cancellation.*—In lines 51 to 55, it is stipulated that the contract may be cancelled by either party—by the insured immediately, and by the company if it gives five days' notice. If the insured cancels the policy the company retains what is called the short rate, which is a higher percentage of the premium than the pro rata return would be. For instance, a policy written for one year would on a pro rata cancellation call for a return of six months' premium to the insured if the company were to cancel in that time, but if the insured cancels the policy, the company is allowed to retain seventy per cent of the actual premium. The five days' provision means five days from the receipt of the notice, and it is customary for the company, in order to be positive that the cancella-

tion notice is received, to send it by registered mail. The framers of the policy intended that, after the company has sent the cancellation notice, the insured would return the policy, and that the unearned premium should then be sent. The New York Court of Appeals has decided that the unearned premium must be tendered to the insured with a notice of cancellation, but this has not been the decision where the question has gone to the United States Courts. It has never been taken up to the Supreme Court, but the Circuit Court has rendered an opinion that the return premium need not be tendered with the cancellation notice.

7. *Mortgages.*—Lines 56 to 59 provide that if there is a mortgagee interest, that interest shall be subject to the provisions of the mortgagee clause. Less responsibility is placed on the mortgagee than on the mortgagor. The mortgagee, after all, has only limited rights in connection with the property and so should not be held to the same degree of responsibility as the owner or mortgagor. It would be impossible, of course, to secure loans on property without a prohibitive rate of interest if the lender were held to the same degree of responsibility as the borrower. Hence, it has been necessary to make a modified degree of responsibility to fit the conditions of the mortgage interest.

8. *Removal cover.*—The insured is responsible for the proper care of his property during a fire as much as he is before a fire occurs. If prudence makes it

necessary while a fire is burning to remove the property which is undamaged, the insured may do this and have the benefit of insurance for five days on the property so removed to a new location. This is a salutary provision which the policy makes for the parties, to encourage the insured to take care of the property.

9. *Procedure in loss settlements.*—Beginning with line 67, down to and including 107, the procedure, in case a loss occurs, is given. This procedure may be epitomized briefly under fifteen different heads. They are as follows: (1) Immediate notice must be given of any loss. The notice must be in writing and the word "immediate" has been considered by the courts to mean reasonable promptness under the circumstances of the case. As many as fifty-three days after a fire occurred was considered by the court to be proper in one given situation. (2) The property must be protected from further damage. (3) The damaged and undamaged personal property must be separated. (4) It must be put in the best possible order. (5) A complete inventory must be made. (6) Within 60 days from the date of the fire, a complete statement must be made to the company as to the time and origin of the fire. This statement must be in writing and signed and sworn to by the insured. (7) He must set forth his interest and that of any other parties in the property. (8) He must set forth the cash value of each item and the loss incurred. (9) He must state any incumbrances on the property that exist. (10) He must furnish a complete list of the

insurance whether valid or not. Policies may be issued whose issuing companies are now insolvent or out of business on the property, but if they have not expired by time limit, they must be set forth just the same as those policies which are in good companies. (11) The insured must have a copy of the description and schedules in all policies. (12) He must notify the company of any changes of title to the property, or in its use or occupancy. (13) A complete statement as to who were the occupants of the building at the time of the fire, must be given. (14) If called upon he must verify the plans and specifications of the building and machinery. (15) A certificate from a magistrate or notary public may be required, setting forth the fact that he has examined into the circumstances of the fire and it is his belief that the loss sustained is an honest one. This is not usually required at the present time.

This list of the duties which are placed upon the insured may seem somewhat formidable but they are not really so. The insurance companies are in business for the purpose of meeting their obligations and obstacles are not placed in the way of a just settlement with the insured. No company could afford to do otherwise because it would soon be obliged to retire from business.

10. *Forms.*—Between the first six lines and line No. 1 in the average policy, there is quite a blank space. This space is commonly known as the space for the "form." The form is a description of the property

that is to be insured under the policy in question. In the preparation of this form, the language of which is not provided for, the agent and broker must exercise skill in order that the insured may be properly protected under the policy that is issued. If a few principles are borne in mind, the preparation of a form is comparatively simple. General terms should be used wherever possible; specific terms must be used where the policy demands them, as in the case of awnings; as few words as possible should be used, but enough to describe properly the property and the object of the policy. It should be remembered that the person who prepares the form and who uses language that is ambiguous will be the party to suffer. For instance, if the form is prepared by the company or its representative and the language is not clear, under the stated practice of the courts in interpreting legal documents, the language will be construed in favor of the party who did not prepare the document. This rule of law is based on the common-sense principle that if one has a chance to use clear language and does not do it, he and not the other party should suffer thereby. It should also be borne in mind that, where the insured employs a broker or prepares the form himself, the use of ambiguous language will be construed against him and not against the company. Two examples of forms are given below:

(1) On Household Furniture, useful and ornamental, Beds, Bedding, Linen, Wearing Apparel, Plate, Plated Ware, Chandeliers and Gas Fixtures, Printed Books and Music,

Pictures, Paintings and Engravings, and their Frames (at not exceeding cost price), Bronzes, Statuary, and other works of Art, and objects of Vertu, Pianofortes and other Musical Instruments, Scientific Instruments, Sewing Machines, Mirrors, Watches, Diamonds, and all other Jewelry in use, Fuel and Family Stores, Tools, Bicycles, Guns and other Sporting Implements, and Utensils, the property of the Assured, or any member of the Family.

(2) $.....On household furniture and other personal property usual to a dwelling, but excluding accounts, bills, currency, deeds, evidences of debt, money, notes or securities; all while contained in the.....building while occupied as.....situate.....

.....

Permission is granted to use kerosene oil stoves, to be filled by daylight only; also to keep on hand not exceeding one quart of gasoline, benzine or naphtha for household use, but the use of gasoline, benzine or naphtha for cooking, heating or lighting is prohibited unless special permission is endorsed hereon.

Permission is given for mechanics to be employed for ordinary alterations in the described premises, but this shall not be held to include the constructing or reconstructing of the building or buildings, or additions or the enlargement of the premises.

Permission granted for the building to remain unoccupied a portion of each year.

The first represents the style where many words are used and the second represents a modern attempt to reduce the language to the least possible limits. It is doubtful, perhaps, whether the language in the latter is quite sufficient to meet the conditions of the standard policy, but these two are furnished as illustrations for comparison.

11. *Clauses.*—There are certain fundamental provisions which both parties to the contract may be willing to embody in the policy. A good illustration of this is the matter of coinsurance. The state provides that the policy may be written under the terms of coinsurance, but if so, that the clause which expresses this fact must be the one provided by the state.

12. *Average clause.*—The standard clause in use with the New York Standard Policy, where the policy is issued with the understanding that the insured shall carry insurance for a certain percentage of the property, usually eighty per cent, reads as follows:

> This company shall not be liable for a greater proportion of any loss or damage to the property described herein than the sum hereby insured bears to ..... per-centum (....%) of the actual cash value of said property at the time such loss shall happen.
>
> If the insurance under this policy should be divided into two or more items, this average clause shall apply to each item separately.

The important thing in the consideration of this part of the contract of insurance is not the language but the thing itself. A great deal of misapprehension exists as to the true aim and purpose of this part of the insurance contract. The clause makes it obligatory upon the insured to carry insurance equal to a certain percentage of the value of the property. Ordinarily this is fixed at 80 per cent. Sometimes in sprinkled risks it is fixed at 90 per cent; very rarely at 100 per cent. There is a common error of supposing that if the policy has the 80 per cent average

clause attached it means the insured will collect only 80 per cent of the amount of the loss. If the insurance equals the amount called for, the clause will have no effect in settling the loss. Perhaps an illustration of the effect of a clause in an actual case will be better than any words of explanation. The property is valued at $10,000 and insured with the 80 per cent clause which makes it obligatory on the insured to carry $8,000 of insurance. The property is damaged to the extent of $4,000 by a fire. When the policies are brought in, it is found that the insured has $8,000 worth of insurance and so will receive the full amount of his loss, $4,000. Let us suppose, however, that when the policies are brought in for checking up, the insurance carried is not $8,000 but $6,000. Now this $6,000 is three-fourths of the amount which the insured agreed to carry and therefore as he has failed by one-fourth to fulfil the obligation which he assumed, he will fail to recover his loss in the same proportion at the settlement. Instead of recovering $4,000, the amount of his loss, he will recover $3,000 which is one-fourth less than the amount of the loss.

The whole aim of the average coinsurance clause is to make sure that practically the whole body of property that may be subject to a loss, is covered by a policy of insurance. The fire insurance business has for many decades been working to the point where a fixed percentage of insurance is called for. The time will come when the state will demand that property shall be insured for at least 80 per cent of its value. The

provision will be based on the simple equity, that the assessment of the fire insurance premium which in many respects resembles a tax, must be subject to the same law to which other taxes are subject, that is, property to be assessed must be assessed for its full value. Without such a provision it is impossible to distribute the fire cost among different policyholders in an equitable manner.

13. *Premium.*—The policy implies that the premium is paid as soon as the policy is issued. As a matter of fact, however, custom governs the payment of the premium. On an average thruout the United States there is usually a credit of two months. Like all other commercial transactions some credit probably would be necessary. Insurance may be wanted on any day during the month by the busy merchant, but as in the case of purchases, he would not expect the bill to be rendered until at least the first of the month. The policy, therefore, whether the premium be paid or not, may reasonably be expected to be in force when it has passed into the possession of the insured. If the premium is unpaid the cancellation notice must be furnished in the same way as tho the premium had been paid. The fact that the company has waived its right to immediate payment of the premium will not enable it to deny liability if a loss occurs.

14. *Loss settlement.*—We have set forth on previous pages the steps which the insured must take in the event of a loss. These need not be recapitulated.

The person who settles the loss for a company is called the adjuster and for strictly business reasons, even if it had no higher motive, the company has every inducement to make its loss settlement promptly, equitably, and we might almost say, liberally. Neither agent, broker nor insured would wish to do business with a company that was a laggard in settling its losses. Hence it follows that a company cannot afford to be behind in any one of these things, if it hopes to continue in the business. The losses under fire insurance policies are settled in 99 per cent of the cases without the necessity of going to court. The man engaged in fire insurance, like the merchant, knows that to continue in business, he must pay his bills and he does so.

15. *Underwriters' associations.*—While the label "combine" has, generally speaking, been removed from fire underwriters' associations by legislatures in the United States, the position is somewhat different in Canada.

During the sessions of the British Columbia Fire Insurance (government) Commission in 1910, some evidence was directed against the Mainland Board of Fire Underwriters, designating the same as a "combine." It was then pointed out by the underwriters that the name was wrongly applied for the reason that in no other manner can equitable and just rates be made, and proper credits given for improvements in risks, or charges made for increases of hazard. Every encouragement is given to each individual property

owner to improve his own risk so that he can obtain a lower rate. He is shown just how his building is rated and advised as to what he can do to make it better and safer. Each change for the better thus secured serves to minimize the fire hazard not only of his, but the surrounding property, and so the whole character of a city or town is gradually improved. In this connection tariff associations, with very carefully prepared schedules for rating all classes of risks, have done more than all other causes combined to improve the conditions, to secure better buildings, improve old ones, to increase the efficiency of the fire departments, to provide better water supply, larger mains, improve streets and alleys, reduce the possibility of fires, increase the facilities for fighting the same and minimize the conflagration hazard, which at the present time exists in every town or city in a greater or less degree.

An insurance company may be willing to fix rates upon its own experience or classification record—and this has been done by many companies—but experience and the records prove that such a policy generally results in catastrophe; as evidence, 1,800 companies have failed in America since 1867.

It unquestionably takes the aggregate experience of a large number of companies to insure absolute protection, for the reason that such enlarged experience offers a better average, and rates based thereon will be more equitable than those based on individual experience. One company may make a profit upon a certain class of risks, while another may lose heavily,

but the average experience of all the companies affords the best criterion on which to base equitable rates. Many merchants, manufacturers and business men find it necessary to estimate their fixed charges from year to year, and it is therefore of great importance that the insurance rates be not only equitable but stable as well. If individual rates were to take the place of association or uniform rates, the fluctuations would be great, and general business would become disturbed and unsettled. If individual rates prevail, those companies which have little or no experience of their own, and having the most meager resources will naturally offer the lowest rates, because they cannot otherwise dispose of their policies, and when the day of adversity comes, it will be found that they have not received sufficient income to pay even their normal losses, and the confiding policyholders, as has often been demonstrated, will find that there are no funds or securities to satisfy their claims.

In 1916, an investigation was held by an Ontario government commission into matters relating to fire insurance in that province. Mr. John A. Robertson, secretary of the Canadian Fire Underwriters' Association, was asked by the commission to explain the essential difference between an ordinary combination controlling the price and output of commodities and an insurance combination.

16. *Unlicensed insurance in Canada.*—The amount of fire insurance carried on property in Canada by insurance companies not licensed to transact business in

Canada was $235,770,000, in 1915, compared with $197,918,000 in 1912. The following table shows how the amount was divided among the various provinces:

Nova Scotia	$5,713,674
New Brunswick	10,733,775
Quebec	76,907,525
Ontario	103,645,877
Manitoba	9,462,290
Saskatchewan	9,030,304
Alberta	6,723,638
British Columbia	13,196,664
Prince Edward Island	16,850
Yukon	340,000
	$235,770,597

The following table shows the nature of the property insured by unlicensed concerns in 1915:

Lumber and lumber mills	$15,488,299
Other industrial plants and mercantile establishments	154,450,371
Stock and merchandise	40,649,711
Railway property and equipment	24,896,076
Miscellaneous	286,140
	$235,770,597

The following table shows the classes of insurers who transacted this business in 1915:

Lloyds' Association	$63,188,168
Reciprocal underwriters	22,109,561
Mutual companies	119,174,939
Stock companies	31,297,929
	$235,770,597

Section 139 of Canada's insurance act regulates unlicensed insurance. It reads in part as follows:

Notwithstanding anything in this act contained, any person may insure his property, or any property in which he has an insurable interest, situated in Canada, with any British or foreign unlicensed insurance company or underwriters and may also insure with persons who reciprocally insure for protection only and not for profit; and any property insured or to be insured under the provisions of this section may be inspected and any loss incurred in respect thereof adjusted; provided such insurance is effected outside of Canada and without any solicitation whatsoever directly or indirectly on the part of such company, underwriters or persons by which or whom the insurance is made; and provided further that no such company, or underwriters or persons shall within Canada advertise their business in any newspaper or other publication or by circular mailed in Canada or elsewhere, or maintain an office or agency therein for the receipt of application or the transaction of any act, matter or thing relating in any way to their said business.

When the act was being revised in 1910, the licensed insurance companies protested against the practice of unlicensed insurance, but the above legislation was apparently thought to be sufficiently protective.

This unlicensed insurance provides some competition but it also allows financially weak companies to write business in Canada. Not infrequently have fires occurred, the losses arising from which have not been paid by unlicensed companies. During an investigation into fire insurance matters in Ontario in 1916, the suggestion was made that the government put a tax on the export of premiums from that province. This would act as a check upon the volume of

unlicensed insurance and, so far as provincial governments are concerned, afford information as to the amount of such insurance carried in the respective provinces. The tendency in Canada is for greater control of unlicensed fire insurance. One or two of the Canadian provinces have imposed a 1 per cent tax upon the amounts of losses recovered from these unlicensed concerns.

REVIEW

A owns a house in your city. He goes away for six weeks, leaving it unoccupied. The house is insured and no riders are attached to the policy. A fire occurs during his absence. Does his policy cover the loss?

In the preceding question, if A had employed workmen to make extensive repairs during the time he was away would your answer be different? Why?

Outline the steps to be taken by the insured in case of a loss.

What is the application of the average clause?

X and Y are engaged in the manufacturing business. X owns the factory and Y is a secret partner in the business. Insurance is taken out on the factory and stock. X is given as the owner. In case of fire will the company raise any objection to paying the loss on either factory or goods?

What is the reason underlying the provision that answers the preceding question?

X takes out a policy on his house. Five months later he sold the house to Y and Y immediately conveyed it to X's wife. Mrs. X wishes you to take a mortgage on the property. What do you wish to know about the insurance policy?

What will you instruct your agent to do with the policy?

CHAPTER V

LIFE INSURANCE

1. *General features of life insurance.*—The term life insurance designates a form of insurance based on the contingency of life. Life insurance has one advantage which has given it a solid basis upon which to rest. It has only one contingency to consider. In all of its forms, even if the policy be payable at the end of an endowment period or a death, the contract is based on the possibilities of death during the period the policy must run. In other words, it is a form of insurance in which there is no doubt as to the sum that must be paid at the end of a period, which is determined by death of the insured or by the lapse of a specified number of years as in an endowment policy. There is but one element of doubt in the transaction and that is when the contingency insured against will occur. Other forms of insurance involve two elements of doubt; whether the thing itself will happen, and if so when it will happen. In comparing life insurance with any other form of insurance this important fact of the solid basis on which it rests must be borne in mind, and if borne in mind much confusion will be avoided.

2. *Early forms of insurance.*—In a very crude

form, there was a real element of life insurance, when centuries ago one departing for the Crusades made provision for a sum of money for his ransom in case he should be captured. If historic records were complete, we should probably find that before the 17th century, policies of life insurance were issued in individual cases backed by individuals or a group of underwriters. The general conditions of life possibly as late as the early 18th century, made life insurance almost impossible as a commercial enterprise. The plagues that followed one another with startling frequency were enough to have deterred anyone who thought of insuring the lives of individuals, or of putting funds into any project for such a purpose. It would be evident to both parties to such a contract that the great devastations of the plagues which cost so many lives made the duration of life a most unstable thing. Without a basic knowledge of the duration of life any form of life insurance at once became the merest gambling and continued in that state until the laws of mortality were developed.

De Witt, in Holland, probably made one of the earliest uses of the principles of life insurance when, in attempting to raise funds for the state, he used the principles of annuities for securing money. The annuity was a form of investment by the individual who turned over his money to the state and received thereon a very fair degree of interest, which interest terminated when the individual died, the state being then relieved of any further obligation. But anything

of this nature was sporadic and hardly ranks as life insurance as we understand it today.

3. *Beginnings in England.*—In England a charter was granted in 1706, to "The Amicable Society for the Perpetual Life Assurance Office." Other organizations came into existence and more or less business was done, but it is now recognized that the true history of life insurance in England began in 1756, when there was put forward "The Society for Equitable Assurance of Lives and Survivorships." The initial success of the Equitable and the feature that really enabled it to survive when all the others went under, was the fact that for many years it did not promise to the beneficiary a fixed payment on the death of the assured, but divided the funds for a given year among all those who became beneficiaries by the death of assured lives in that year. The amount received by the beneficiary naturally varied with the number of deaths, but with the small experience concerning insurance which at that time existed in the world, any other method would have wrecked the Equitable as it did the previous societies which had attempted life assurance. In due time the Equitable grew in wealth and was able to promise a fixed sum on the death of the insured and this society, while never doing a large business, as we think of business today, nevertheless has continued successfully down to the present time.

After the founding of the Equitable many other companies were organized. Unfortunately there was the same element of gambling connected with many

of these enterprises as with other forms of insurance, and it was not until about 1849 when the stiffened laws regarding life insurance companies came into existence that stability was given to the business. These laws were placed on the statute books as a result of a few very prominent failures among the life insurance companies. But of course many companies honestly carried out their obligations from the beginning and were not affected by the disasters which overtook those less prudently and less honestly managed.

In 1844, it is estimated that there were in Great Britain over 140 different assurance companies and societies organized for the purpose of insuring lives.

4. *In the United States.*—There were probably not one hundred policies, so it is estimated, of life insurance in force in the United States in the beginning of the 18th century. These were purely underwriter's policies. In 1754 in Pennsylvania, the Presbyterian church organized a society for insuring the lives of its ministers. This society was not organized wholly on strict insurance principles because it depended somewhat for its income, in the beginning at least, on funds which were given to it in addition to the sums charged the insured. But that phase passed away in due course and this unique experiment in life insurance as it has been called, is still in existence and the company is doing a good work. In 1843, the Mutual Life Insurance Company of New York, issued its first policy and that may be considered as the real beginning of life insurance in the United States. The business

profited by the experiments which had been worked out or tried in Great Britain, tho many of the new companies did not derive as much benefit as possible from this experience. The business, however, started in this country on a foundation that was much more secure than that from which the pioneers in Great Britain had been obliged to work. There was a fairly quick growth down to the beginning of the Civil War. Contrary to expectations, in the period of the Civil War, the business did not decrease, altho the southern part of the country was not available for life insurance work. But beginning two years prior to the panic of 1873, many of the weaker companies began to retire, and from that time until 1880 a process of weeding out occurred which resulted in the disappearance of some ninety companies. The whole condition was improved by this clean-up, and from that time until 1905 the business went on from one degree of success to another. In 1905 the Armstrong Investigation took place and as a result of its disclosures the laws of various states were somewhat stiffened—too much so, many think. But every candid historian of the business would probably admit that the legislation of 1906 placed the business of life insurance on so solid a foundation that its subsequent success has been greater than it possibly could have been without these laws. One result of the crisis of 1906 was the formation in the South and West of a large number of new companies; something like two hundred companies have been organized, operating mostly in that field. Very

few have come into the middle Atlantic or northeastern states. As a matter of fact, less than fifty companies operate in the State of New York. These small companies have accomplished an excellent work. Many of them have made mistakes; many have retired but, on the other hand, they have done a very useful work in spreading a knowledge of life insurance. Many have built up a very successful business and are a distinct accession to life insurance.

5. *Insurable interest.*—In its early days the same difficulty immediately associated itself with policies of life insurance as with those of marine and fire. People thought it a new scheme for getting rich, and it was possible to take out a policy of life insurance on the life of an individual in whose life one had no interest and even with whom the beneficiary had no acquaintance. The illness of any noted individual or sovereign served as an excuse for securing policies of insurance which, of course, were nothing more than gambling ventures. So great an evil did this grow to be that the Gambling Act was passed in Great Britain in 1774. This act expressly forbade anyone taking out insurance on another's life, unless they had an insurable interest therein; it also applied to all other forms of insurance except marine, which had been made subject to a similar rule in 1749.

To prevent any misunderstanding let it be emphasized that it is impossible to take out a policy of life insurance on another without that person knowing it, even tho an insurable interest exists. One may con-

duct the early negotiations without his knowledge, but the person insured will, of necessity, have to sign the application and pass the medical examination. Much of the preliminary work, all of it in fact, in the case of children, may be done by one having an insurable interest.

An insurable interest is precisely the same thing as it is in property insurance, only in this case, it is so related to a life that the loss of that life would mean a loss measurable in money value to the person who seeks to have the life insured. The wife, for instance, has an insurable interest in the husband because he is obliged by law to support her. Parents have an insurable interest in the lives of the minor children because the parents are entitled to the wages of the child until the age of twenty-one. Where relationship exists coupled with either an obligation to support or even, if the obligation does not exist, where the fact of support exists, as a brother supporting a sister, there is an insurable interest.

6. *Beneficiary.*—Having said so much in setting forth the insurable interest, we must now emphasize that a person insuring his own life may choose as the beneficiary of a policy almost anyone he pleases. It is natural to suppose that one would never choose to carry a policy of life insurance for the benefit of another individual unless there were some good reason for doing so, either to protect the family or to protect an individual from whom one has secured a loan. Such a loan would be paid in due course of affairs if

the individual lives, but might not be paid if he dies, and therefore the borrower may protect the lender by the policy of insurance. So while it may be stated with all frankness that, in the best sense of the word, one may choose as a beneficiary whom he will, it is obvious that if someone should be chosen as beneficiary who had no insurable interest, and that those who had an insurable interest were left unprotected, there might be occasion for some suspicion as to the necessity of the transaction. As a matter of fact, however, no trouble arises apparently from this cause. Such few cases as have arisen have had some form of crime connected with them and furnish a special chapter in the history of criminal law. Except as showing what the individual may do to secure funds, such cases are not of much moment in life insurance.

7. *Beneficiary under Canadian law.*—The Canadian laws regarding beneficiaries are based upon the broad principles prevalent in most other countries. They are complicated in Canada, however, by the legislation of Quebec province, where there are a large number of French speaking people. Quebec has a wives' and children's act, as has Ontario, and the other provinces have articles of their acts concerning preferred beneficiaries. Preferences are not so numerous in Quebec as in Ontario. These are in the case of a man, his wife, his children and his wife's children; in the case of a woman, her children. The beneficiaries may be appointed either by the policy itself or by appropriation by a subsequent document

or by will. A wife may insure her life for her children's benefit, or appropriate a policy to them without the consent of her husband, this constituting a departure from the common law governing consorts. A policy in favor of a preferred beneficiary cannot be changed without his consent, except in favor of another preferred beneficiary. It may be assigned or surrendered with the consent of all the beneficiaries if they are of age. The proceeds of the policy cannot be seized either by the creditors of the assured or those of the beneficiary.

When preferred beneficiaries die before the assured, various circumstances must be considered in determining who is entitled to the money. When such beneficiary is a child his descendants take his share whether an apportionment has been made or not. When several children are beneficiaries and no apportionment is made, if any of such children predecease the assured, without issue, accretion takes place in favor of the surviving children. When the assurance is in favor of a wife and a child or children, also without apportionment, if the wife dies before the assured, accretion takes place in favor of the child or children, and if all the children predecease the assured, accretion takes place in favor of the wife. When the sole beneficiary in whose favor the assurance exists, whether wife or child, or all the beneficiaries, predeceases or predecease, the policy reverts to the assured, save in the case of a child leaving issue as before stated. The benefit of any share in an apportionment reverts to the

assured, save in the case of a child to whom the policy was apportioned dying with issue. It is to be noted in all these cases that if the wife is the sole beneficiary, or an apportionment exists in her favor, it does not matter whether she leaves issue or not, for the policy or her share, as the case may be, reverts to her husband.

Trustees may be appointed by the assured to receive the policy moneys in trust for the beneficiaries, as in the other provinces. If no trustees are appointed, payment is made to the beneficiary or beneficiaries named. The shares of minors, if there is no trustee, are paid to the executors of the will of the assured, and if there is none, to their tutors (or guardians).

Another feature of Quebec law is peculiar and that is the right to change the beneficiary. If the beneficiary is a preferred beneficiary, wife or child, the assured may make whatever changes he likes within the family circle. In that respect Quebec does not differ from the other provinces of Canada, but if the beneficiary is outside this circle—father, brother or stranger—it depends on whether or not the beneficiary has accepted the contract made in his favor. There is nothing in the law of insurance regulating this point, so as insurance is a contract we fall back on the common law of contract. Article 1029 of the Canadian Code says:

> A party may stipulate for the benefit of a third person, when such is the condition of the contract which he makes for himself, or of a gift which he makes to another; and he who makes the stipulation cannot revoke it if the third person have signified his assent to it.

Quebec has not the vested interest doctrine which prevails in the majority of the United States, but if a beneficiary has accepted the contract made in his favor it is irrevocable, and a new beneficiary cannot be substituted without his consent. It is therefore always necessary to inquire whether or not the beneficiary has accepted. The Canadian courts have decided that acceptance by a beneficiary need not be in writing at all, but may be made tacitly. That is to say, his conduct and actions may be sufficient to constitute acceptance. The only safeguard for the company is to take such precautions as it can. For instance:

Require a solemn declaration from the assured, stating that the beneficiary named in the policy did not know that he was made a beneficiary, and that he never had possession of the policy which always remained in the hands of the assured; and if the assured cannot say that the beneficiary did not know of his having been so appointed, to at least ask him for a solemn declaration, stating that the beneficiary never accepted nor signified his acceptance of the benefit of the stipulation, either expressly or tacitly. Another article of the Canadian Code (1145) says that payment made in good faith to the ostensible creditor is valid, altho it is afterward established that he is not the rightful creditor; so where such a solemn declaration is made it is understood that a new beneficiary, assuming that he survive the assured and no further change be made, is, under the circumstances, an ostensible creditor, and payment to him will free the insurance company.

These few notes will give a broad idea of the somewhat complicated legislation in Quebec province. Its interpretation has exercised the talents of the best legal men in Canada, including Mr. J. Armitage Ewing, K. C., of Montreal, to whom the authors are indebted for the foregoing information on the subject.

8. *Statistics.*—The Report of the Insurance Department of the State of New York giving the statistics of companies doing business in that state as of December 31st, 1915, will, because of its authoritative character, give some information which will enable us to appreciate the stupendous business represented by life insurance.

(a) The assets were $4,850,000,000; representing an increase in one year of $213,000,000.

(b) The liabilities were $4,586,000,000, this not including special funds of $109,000,000, and leaving a surplus of $154,000,000.

(c) The income was $925,000,000, an increase of $51,000,000 over the preceding year.

(d) The disbursements were $713,000,000, which was an increase of $69,000,000 as compared with the preceding year. The disbursements were roughly subdivided as follows: Claims $288,000,000; Lapsed and Surrendered Policies $113,000,000; Dividends $106,000,000; Commissions $57,000,000; Salaries and Medical Examiners' Fees $58,000,000.

(e) The record of policies terminated for the year is of interest as it shows the different causes. The record was as follows: Deaths 77,000; maturity 32,000;

expired 97,000; surrender 185,000; lapsed 262,000.

(f) The classification of policies for the companies doing business in New York State showed that the whole life policies numbered 5,213,000, the endowment policies 2,399,000, all other policies, including term and irregular policies, 675,000. These do not include, of course, policies issued by industrial companies. The number of such policies in force were 30,000,000, representing a policy value of insurance of $4,000,000,000.

9. *Life insurance in Canada.*—In Canada, according to official statistics for 1915, the business of life insurance was transacted by 44 active companies, of which 26 are Canadian, 7 British, 1 Colonial, and 10 of United States origin. During that year and the latter part of 1914, the life insurance companies were faced with difficulties such as have never before been experienced in Canada. On the outbreak of war, they were confronted with an immediate depreciation in all classes of securities, a complete demoralization of security markets, and a prospective large increase in claims arising out of the war.

While these difficulties were recognized during the latter part of 1914, the seriousness of the conflict was perhaps not fully realized until 1915, and with the indications which the events of that year gave of a prolonged struggle and of the necessity of further Canadian contingents, the companies were forced to modify their practices in respect of the insurance of enlisted men.

Notwithstanding the difficulties arising out of the war, the total amount of policies in Canada taken during 1915 was $221,119,558, which was greater than the amount taken in 1914 by $4,113,042. The respective amounts effected in 1915 were: Canadian companies, $121,033,310; British companies, $5,727,313, and United States companies, $94,358,935. Thus the amount taken by Canadian companies exceeded that taken by the British and Colonial and United States companies together by $20,964,562.

The total amount of life insurance in force in Canada at the end of 1915 was $1,311,616,677, which shows an increase of $69,456,199 over that of the previous year, being distributed as follows:—

	Amount in Force
Canadian companies	$829,972,809
British and Colonial companies.	58,087,018
United States companies	423,556,850
Total	$1,311,616,677

With its population of about 8,000,000, it is generally conceded that Canada's people are seriously underinsured. There are in that country not less than 3,000,000 insurable men and women, mostly men. If each were insured for $1,000, the sum of $3,000,000,000 would be represented, whereas the companies doing business in Canada have at present in force a little more than $1,000,000,000, covering only about one-sixth of those who could and should avail themselves

of the service and help of life assurance. In their effort to overcome this national disability, the life insurance companies have been somewhat hampered by the tendency of the provinces to place unduly heavy imposts upon the premiums collected within their several jurisdictions, but it is hoped that the legislative need may pass and that many of these tax burdens will eventually be removed. The Canadian federal government has recognized that to tax life insurance premiums is a penalty on thrift. In 1916, when framing legislation for the taxation of business profits, the federal government exempted the business of life insurance. The provincial governments of Canada have not yet come to that desirable point.

10. *Procedure.*—As in the case of fire insurance, it will be well to consider the successive steps in order, so as to obtain a clear idea of the whole transaction. These steps are (1) the application for insurance; (2) the medical examination; (3) the preparation of the policy; (4) the delivery of the policy and collection of the premium; (5) the continuance of the policy; (6) the payment of the loss.

11. *Application.*—Few persons apply for life insurance without solicitation. Indeed, some years ago the feeling against one who applied for life insurance was so strong that it was crystallized into the saying: "If a party applies for life insurance he should be examined three times by a physician and then rejected." One would never apply for life insurance, it was felt, unless he knew that there was something the matter

with him and that he wished very much to protect some interest by means of the insurance policy. The view, however, was undoubtedly based on a misunderstanding.

Human beings do not indeed, go around expecting to die. Life insurance, unfortunately, in its beginning, associated itself almost entirely with death. The object of taking it was held up to the individual as a provision which he ought to make for the benefit of those whom he might leave behind; in other words, the family. So insistent was this note that the phrase "life insurance is one of those things where you must die to win," became common. This whole attitude is now passing away. We are coming to look upon the insurance of life more as a commercial transaction and, as we do so, we shall probably place it upon more solid foundation. This view is bringing into the subject an element of danger, but that danger can be guarded against, and is small compared to the large benefits which will be derived from the increased use of life insurance, because it will be regarded as a commercial transaction. In a very recent instance, a firm was sending abroad a representative to examine into certain matters in Russia and part of the compensation offered was a life insurance policy taken out and paid for by the firm. This illustrates the modern view of the matter.

The great majority of the persons who insure their lives do so because they are solicited by the representative of the company. Attempts both in England and

in the United States to sell insurance without solicitation have not been very successful in comparison with the large business of companies which have employed agents to sell their policies.

12. *Form of application.*—If there ever was a time when the oral application for life insurance was good, it passed away long ago and only written applications are accepted. The essential features of an application are: Name and residence of the applicant, place of business, address, date of birth; this given for the day, the month, the year, and also age at last birthday; place of birth, including town or city, state or province; country; present occupation; any contemplated change of occupation; any connection with military, naval organizations; name of beneficiary, residence, relationship or insurable interest in the proposed life of said beneficiary. There are also such questions as: Do you wish the privilege of changing the beneficiary provided policy has not been assigned? Amount of insurance applied for, plan, premiums, how to be paid, as, annually, semi-annually or quarterly? Do you wish the privilege of waiving the premium in case of permanent total disability? Are any negotiations pending for any other insurance? Have you been examined for life insurance and rejected? There may be a further agreement that, after the policy is issued, one will not engage in certain extra hazardous occupations or employments. This includes a variety of occupations such as retailing intoxicating liquors, submarine labor, the

manufacture of highly explosive substances. These are sufficient to indicate the character.

None of these phases call for any special comment, with the exception of one or two which contain more human interest than the others. Take the question of age. It has proved, in dealing with hundreds of thousands, impossible to obtain exact statistics in regard to the matter of age. People are apt to report their ages in even numbers, at certain periods of life. There is a tendency to make oneself older and perhaps at a certain period, to make oneself younger without any real intention to deceive. An investigation into many thousands of cases, shows that the cases where the age was understated were counterbalanced by those where the age was overstated; in other words, so far as payment of premiums was concerned the companies did not seem to be losing any money. Like all other forms of insurance, the transaction is based on absolute good faith between the parties, and any misstatement made purposely would at once cause the company, on discovering it, to cease negotiations with the persons in question.

13. *Medical examination.*—The next step in the transaction after the application has been received, and the company decides from that evidence to go further, is to have the medical examination. The medical examiner stands to the life insurance company in the same relation that the inspector does to the marine and fire insurance company. He is the one on whose judgment the great body

of risks are written, and for this reason it is, perhaps, needless to state that his ability must be unquestioned. It is not merely a knowledge of medicine as it may be taught in the schools or learned in daily practice, but a special knowledge which is acquired in the examination for the passing of the risk for purposes of life insurance, and from a knowledge of the death claims which have originated on the lives of those who have been passed by the medical officers. In most of the companies the medical examiner's reports are divided into two parts, (1) statements to the medical examiner, and (2) the medical examiner's remarks. The first are the replies to a series of questions which the examiner asks. Briefly epitomized, they may be set forth as follows: Your full name. Are you married? What illnesses, diseases, etc., have you had since childhood? A statement of the physicians who have treated you; or, whom have you consulted in the past five years? Are you in good health?

It is evident that the phrase "good health" has a variety of meanings and one may be much sub-standard as compared with another person and still consider himself in good health. This the examiner will check by the other information brought out during the examination.

14. *Use of intoxicating liquors.*—The question of the use of intoxicating liquors forms a very important part of the information which is sought to be obtained. To illustrate, note the following questions which are asked. (a) Have you ever been engaged in the sale

or manufacture of liquors? (b) Have you used them during the past year? (c) If you have, what has been your daily average? (d) What was the maximum amount used in any one day? (e) Have you been intoxicated during the past five years? (f) Have you ever taken treatment for alcoholic or drug habit? (g) If you are a total abstainer, how long have you been so?

It will be noted from the minute detail of these questions that they are deemed of primary importance by the medical examiner. In the early days of life insurance, the question was probably comparatively simple and only asked the applicant if he used intoxicating liquors. But this was found to have so many meanings with the different applicants that it became necessary to develop a series of questions in order to call forth the exact information that was desired.

In regard to the use of drugs, it might be pointed out that they occupy a somewhat different moral status from the use of liquors. Anyone will state without question whether he does or does not use intoxicating liquors, but the use of drugs is a habit which one instinctively seeks to conceal, and it is deemed far more difficult to obtain information concerning that matter than concerning the use of liquors.

While heredity is not deemed of so much importance as it was in the early days of life insurance and up to a few years ago, it does have a certain bearing, especially in connection with certain diseases, as tuberculosis. Questions concerning such disease will usu-

ally deal not merely with the individual himself, but with the members of the household who are afflicted with that disease.

In regard to the family, information is collected as to the age of the parents at the time of death, if not living, and the same regarding the brother and sister, also in regard to grandparents.

15. *Medical examiner's report.*—The medical examiner is then called upon to fill out a report based largely on the information gathered directly, or by observation, at the time of the examination. The report closes up with the direct question as to the examiner's willingness to recommend the applicant for insurance. The report is then duly certified and passed on for the inspection of the medical officer at the home office.

16. *Is medical examination necessary?*—In the beginning of life insurance there was no medical examination. There was probably little necessity for an examination, since there was no attempt to do business over a wide extent of territory and business was local. It must have been a rare case in those days and indeed for some decades after the business was founded, when any applications for insurance could not be well certified to the trustees by persons with whom they were acquainted and on whose judgment they relied. When the companies began to branch out and the business became larger, it was necessary to protect their interest, and this coincides with the insured's interest, by a medical examination. Such

an examination is not indispensable and it is omitted, in certain cases where the number of entrants is sufficient to permit of the principle of choice not being exercised against the company. Any company could probably insure safely the first thousand or second thousand or more men who pass its door. The difficulty is that without medical examination the choice would be steadily against the company. Those who had some reason to feel that their lives were sub-standard, would seek insurance and not those who were confident of their good health. In the now developing field of group insurance as it is called, where all the employes of a plant may be insured, admittance to the company is permissible without medical examination because the number is so large that the company secures a fairly average selection of lives in the whole group.

Our knowledge of the human body has led to the conclusion that the result of a medical examination may be relied upon for about five years. After that period insured lives tend to approach more nearly to the normal level of the great body of uninsured lives.

REVIEW

Mention some of the early movements in the life insurance field.
Trace the development of life insurance in the United States.
Do you know what the Armstrong investigation was?
What is an insurable interest in life insurance?
In group insurance, why may the company dispense with medical examination of the risks?

CHAPTER VI

MORTALITY AND INVESTMENT EXPERIENCE

1. *Factors in the premium.*—In life insurance, the premium is commonly expressed by the amount charged for one thousand dollars of insurance for ordinary policies, and by smaller units for industrial insurance. The two great factors which determine the premium are mortality and the interest received from investments.

2. *Mortality tables.*—Newsholme described the mortality table as the picture of a generation of individuals passing thru time. Mortality tables are based either on statistics of the population as shown by the census returns, or on statistics of the life insurance companies, based on their own experience. The first table was compiled by Halley, the astronomer, in a paper for the Royal Society. He used statistics from Breslau, Silesia, where statistics of birth and death had been kept from a very early period. Halley's table lay buried for many years in the journals of the society and was probably never used by any insurance company. The first table that was actually used by any insurance society, is known as the Northampton Table, and was based on the statistics of some parishes in Northampton. This table became justly famous, altho it has been entirely superseded.

Another table, of far greater accuracy than the Northampton, is the Carlisle, based on the statistics of some parishes in Carlisle, England. The number of lives considered was less than fifteen hundred, but the table has proved to be remarkably accurate even with the changes that have taken place since the table was compiled more than a century ago.

A table based on the statistics of population is not satisfactory to an insurance company which has been in existence for any length of time. It does not represent experience in dealing with picked or chosen lives. The insurance companies have not devoted much time to the sub-standard life, as they have found a sufficient number of standard lives to build up their enormous business. As soon as the companies secured a sufficient amount of experience on which to base accurate statistics, they dispensed with statistics taken from other less reliable sources.

3. *What is a mortality table?*—In the somewhat vivid picture which described it as "a generation of individuals passing thru time," we catch a fairly accurate idea of what the table aims to present. It traces a group of individuals, taking their lives at an assumed period, until the entire group have passed away. It shows the number at the beginning of the period and also the number that pass away each year, and with these two factors it is easy to show the probability of dying within the year or of surviving within the year.

4. *American experience table of mortality.*— The

table in common use in the United States is the American experience table of mortality, based on statistics taken from the experience of the Mutual Life Insurance Company during a certain period in its history. The table was prepared by the then actuary, Sheppard Homans, and altho the work was done at a comparatively early period in the history of American life insurance, the experience was so true and the work so accurate that the table has stood the test of time remarkably well.

5. *Illustrations.*—Let us illustrate what the table shows. It assumes that at the age of ten years there are 100,000 lives and year by year it sets forth these four things: (a) the number of living at the beginning of each year; (b) the number dying each year; (c) the yearly probability of dying; (d) yearly probability of living or surviving. The last age represented on the table is ninety-five years. There was no experience to show any insured life living beyond ninety-five. There has been, of course, since that time actual experience in regard to insured lives beyond that age.

It is not necessary to reproduce the entire table; our purpose will be served by showing it at ten-year intervals.

Age	No. Living at the beginning of the year.	No. Dying during the year.	Probability of Dying thru the year.	Probability of Living thru the year.
10	100,000	749	.007490	.992510
20	92,637	723	.007805	.992195
30	85,441	720	.008427	.991573

Age	No. Living at the beginning of the year.	No. Dying during the year.	Probability of Dying thru the year.	Probability of Living thru the year.
40	78,106	765	.009794	.990206
50	69,804	962	.013781	.986219
60	57,917	1,546	.026693	.973307
70	38,569	2,391	.061993	.938007
80	14,474	2,091	.144466	.855534
90	847	385	.454545	.545455
95	3	3	1.000000	.000000

6. *How the table is used.*—Let us assume that a person aged forty desires insurance for one year, two years or any number of years. At age 40, the table shows that there are 78,106 persons living. The number that will pass away in that year is 765; hence it would be $\frac{765}{78,106}$ for one year. For two years it would be the number 765 plus 774, which is the number passing away in the second year, over the number 78,106 as a denominator, or $\frac{1,539}{78,106}$ and for five years it would be $765 + 774 + 785 + 797 + 812 = \frac{3,953}{78,106}$

No data upon insurance experience were available, up to late in 1916, from which to ascertain the rate of mortality experienced to that date in the European War. The general effect of war claims upon the mortality as a whole may, however, be observed by comparing the actual claims of the year with the expected, by the Standard Valuation table. Figures of nine Canadian companies for the year 1915 show that the total mortality, including war claims, was remarkably favorable in every instance, the ratio of actual to expected ranging from 42.6 per cent to 72.9 per cent,

while for eight of the companies combined, it was 58.4 per cent. The net loss under war claims for the nine combined companies was 13.3 per cent of the expected claims. The gross war claims for the nine companies combined were .134 per cent of the mean Canadian business in force. The corresponding figures for the Mutual Life of New York were .107 per cent for Canada and .196 per cent for the combined business in all countries engaged in the war. The gross Canadian claims incurred by the nine companies were $5,834,822, of which $900,869, or 15.2 per cent were due to the war.

The general consensus of opinion among British and Canadian actuaries, as reflected by the extra premiums charged to cover the war risk, is also in accord with the view that a much heavier death rate than five per cent per annum may be anticipated. At the outbreak of the war, the extra premium recommended by the British Life Offices' Association in connection with new assurance was 7 per cent for the combatant branches of the service. This rate was shortly afterward increased to 10, and later on, it was decided to leave the question of extra premium to the individual judgment of each office.

In an instructive address to the Actuarial Society of America in 1916, Mr. Arthur B. Wood, actuary of the Sun Life Assurance Company of Canada, discussed the European war risk with particular reference to the practice and experience of Canadian companies. He said:

It is generally conceded that the statistics of previous wars are no indication of the mortality rate likely to be experienced in the present European war. Such information as is thus far available undoubtedly indicates that the rate of mortality has already been very high, and no one can predict with any degree of confidence what the future experience will be.

Considering the uncertainty attached to the question it is a wise precaution not to fix the extra premium definitely in advance when issuing a policy, but to retain the right to readjust the rate from time to time according to the judgment of the company.

7. *Interest return.*—A life insurance company bases its calculations upon the fundamental fact that every policy which it issues must be paid if the policy be carried to a conclusion. The experience of lapsed policies is of no value to the company and indeed its effect on the whole business of life insurance is wholly an uncertain one, so any possible gain from that source the company does not and should not consider. Its calculations are based on the payment of the amount for which the individual is insured, either at the death of the insured or at the end of the insurance period in an endowment policy.

It stands in respect to the endowment in the position of one who knows that in twenty years he must meet a note for $1,000 and must collect, during that interval, such a sum of money as, set aside and permitted to increase at a certain rate of interest, will meet that obligation at the end of twenty years. Now the life insurance company, as it insures large numbers of persons, many of whom die before the policy period of

expiration, meets its obligations as they fall due, by adjusting its charges on the basis of the mortality table and an assumed rate of interest less than it may reasonably expect to earn, but yet so near as to what it may expect to earn that its premiums will not be unduly high. Competition among the different companies, it may be added, is quite sufficient to take care of this factor of the premium fixing. In the early history of the United States when the rates of interest ran very high (6 per cent when they were 4 per cent in other countries), an undue increase was assumed from this source and a decade or two was spent by the companies in working to a more solid foundation. Probably the general assumption now is that the company will earn on its invested funds 3½ per cent and it so estimates in making its premium rates. As a matter of fact, the companies earn more than this sum and it is not improbable that the time may come, with the enormously increasing demand for capital, when 4 per cent will again become a fixed rate of interest for which the companies may assume a return from their invested funds. However, under the system of annual dividends which prevails in the UnitedStates it is almost immaterial what rate of interest a company may assume so long as the amount be within the line of safety. If it assumes a rate more nearly to what it will earn than some other company, the other company can even up by making its annual dividends somewhat higher.

8. *Policy conditions.*—The general conditions of

policies may be briefly summarized. The beneficiary may, if the right has been reserved, be changed by the insured. For many years this right did not exist but the beneficiary once having been named, a change could not be made by the insured without consent of the beneficiary. If the beneficiary dies before the insured, the policy vests in the insured.

There are two classes of policies: participating and non-participating. The first shares the dividend, the second does not. It is purely a question of choice with the individual which type of policy he prefers to take. The non-participating policy has the advantage of a fixed payment according to the terms of the policy, subject to no reduction during the period payment of the policy, while, in the case of the participating policy the insured shares in dividends as the company is able to declare them.

9. *Suicide.*—If committed within one year from the time the policy is issued, suicide voids the policy, but after that time the policy is incontestable. In connection with the question of suicide it may be of interest to note that the attempt to issue policies without a restriction as to suicide, say one year, has proved to be unwise, and it is not often done at the present day.

10. *Premiums.*—Advance payment according to the time arranged, as annual, semi-annual or quarterly is the rule for premiums. They are payable at the home office of the company or to any designated agent. A period of grace of thirty-one days subject to an in-

terest charge is usually granted after the first premium has been paid. Should the insured die within this period, then the premium due would be deducted from the payment to the beneficiary. The policy immediately ceases if the payment is not made on or before the end of the period of grace.

11. *Dividend distribution.*—There are several methods of distributing dividends. They may be paid in cash, they may be used toward paying the premium on the policy, or they may purchase more insurance or be left to accumulate. Usually, if the insured has not manifested any expressed wish in regard to the matter, the company will apply the dividends in a certain manner as set forth in the policy.

The average policy today is free from any restriction as to residence or travel. The same is true in regard to occupation unless one were engaged in employments which are admittedly hazardous, including warfare. Naturally if one should enter upon such an employment the proper thing to do would be to notify the company in order that an additional premium may be arranged, should the company care to continue the insurance.

12. *Assignment.*—If the policy is assigned due notice thereof should be given to the company.

13. *Reinstatement.*—Provisions are made for reinstatement of the policy within a certain number of years. Having insured a life, the company desires to continue the policy in force, and that is the reason for the provision of grace and the reinstatement privilege.

Usually there are various options which the insured may exercise after the policy has been in force for a certain number of years, generally three. It is considered that that period is necessary before the cost of securing the insured life has been overcome, and the reserve set aside is of some value to the assured life.

In Canada, the clauses used by all companies after January 1, 1911, with four exceptions, require evidence of insurability as a condition precedent to reinstatement. The clauses of the four excepted companies require merely evidence of good health. The policies of fourteen companies permitted reinstatement at any time; the others within two, three or five years from date of lapse.

In interpreting the term "evidence of insurability" in cases of reinstatement, most companies have applied the same test to military service as in accepting applications for new insurance, and this practice in the opinion of the Canadian department of insurance conforms with the provisions of the act.

Twenty-four companies in 1915 granted reinstatement on being satisfied that the applicant did not intend to enlist. The other companies incorporated the war clause in use for new companies' policies in policies reinstated.

14. *Loans.*—It was Elizur Wright of Massachusetts, probably as able a life insurance man as this country has ever produced, who secured for the insured the right to an interest in the reserve. Before

his time one who allowed his policy to lapse, altho it may have been in force many years, lost all that he had put into it. Wright established the fact that against the assured's policy there was held a certain reserve which grew larger and larger as the time of expiration approached, and that, to deprive the insured of all this when he was in many cases compelled to abandon his insurance was unjust. This, of course, is now an accepted principle in the insurance world. Now, instead of abandoning the policy, there has grown up the feature of loaning against this reserve. Loans did not assume large proportions until the panic of 1907 in the United States. Apparently then the knowledge became quite prevalent that most of those carrying life insurance had a substantial asset in the form of this reserve, and as the company was obliged to loan them on demand they promptly proceeded to borrow from the company. It is evident that as the policy has been taken out for the beneficiary's use, this borrowing privilege defeats the very purpose for which the insurance was taken out, which was to protect the beneficiary. These loans are moreover rarely repaid. This is surely one of the most undesirable practices in the field of insurance, as it very often leads to a complete surrender of the policy. A great many remedies have been suggested from time to time but no effective method of meeting this evil has been devised. It is possible that state law will eventually require at least, the reduction of the loan by certain annual payments thru a series of years.

The policy usually has a table setting forth its value at the end of periods if it be surrendered or if a loan is desired on the policy.

15. *Policy loans in Canada.*—The policy loan has been the subject of much discussion in Canada. The following table shows the total assets and the loans, including premium obligations, upon policies of Canadian life companies, at five-year intervals since 1890 and the proportion which these loans bear to the assets:

CANADIAN LIFE INSURANCE COMPANIES

Year	Total Assets	Loans on Policies	Per-centage
1890	$20,740,444	$1,716,561	8.28
1895	35,323,297	3,582,862	10.14
1900	59,504,066	6,014,022	10.11
1905	102,438,415	9,679,244	9.45
1910	170,804,631	20,409,223	11.95
1915	274,273,018	39,311,402	14.34

This shows that, rapid as has been the growth of the assets, the increase in loans on policies has been nearly twice as great and that the proportion is still rising.

The deductions to be drawn from an analysis of the Canadian situation are that policy loans are rapidly increasing and in view of the United States experience, they must be expected to rise higher; that in years of financial stringency, exceptional calls will be made upon the life insurance companies and that during financial panics, they must be prepared to find cash, at short notice, for large amounts.

At various times, legislation to restrict the volume of loans on life insurance policies, has been suggested but, as has been pointed out by Mr. R. W. Barton, A. I. A., an English actuary,

> Life companies see tragedies in families at the death of the breadwinner due to insufficient and neglected assurance. Banks witness tragedies in life on the failure of their customers in business. Each, by giving such advice to the public, as their experience suggests, can help those willing to learn, to avoid the dangers that have caused disaster; but to try by legislation to stop borrowing, or the use of savings, is as hopeless as to try to regulate currency by government fiat. History proves that neither human nature nor currency has ever been made good by act of parliament. With this in mind, only if the dangers of the present system are shown to be insurmountable, would the Canadian companies be justified in seeking drastic legislation to restrict policyholders' right.

The policy loan situation in Canada may be briefly summarized as follows:

For the policy loan. 1.—Business men use life insurance companies as custodians of surplus earnings, to be available when necessity requires, or as a provision of old age.

2.—The policy loan is at least a great convenience to the policyholder, and has probably come to stay.

3.—The loan may be used to keep policy in force, by paying premium due.

Against the policy loan. 1.—A solvent life insurance company might fail as a result of policy loan provisions in the insurance act.

2.—Life companies are called on to make loans when investment opportunities are best.

3.—Some policyholders, owing to interest rate being stated in policy, can borrow more cheaply than others and a single policyholder may have to pay different rates on different policies, causing much confusion.

4.—Policyholders do not always pay back their loans but borrow more, creating a dangerous condition.

5.—The policy loan is often the first step to the total surrender of the policy.

The following suggestions for reducing the volume of policy loans have been made in Canada from time to time:

(1) Notice of intention to borrow should be given by the policyholder, except when loan is required to pay premium to keep policy in force.

(2) Government should protect policyholders against themselves by making it more difficult to borrow on policies.

(3) No loan whatever should be granted on a life policy, covering dependents, except to pay premiums; other loans to be treated as a commercial transaction.

(4) A partial remedy would be to educate policyholders to realize the seriousness of mortgaging the protection they have created for their dependents.

16. *Manner of settlement.*—There are various ways

now of paying the beneficiary. The feeling is growing that instead of permitting the policy to be paid all in one sum it is better to have it paid over a series of years, thus providing a fixed annuity. This is especially true if the beneficiary is one who is not accustomed to handling even moderately large sums of money at one time. He may on receiving them have quite a false idea as to the amount represented. Undoubtedly in many cases where the policy has been paid in a lump sum, the real purpose of the insured, to protect the beneficiary, has been defeated.

REVIEW

What mortality table is in use in the United States?

What argument in favor of paying a policy by instalments may be advanced?

How were the various mortality tables computed?

X takes out a policy of insurance with his wife as beneficiary. His wife dies and later X dies, having named no new beneficiary. He is survived by one daughter. Who receives the benefit of the policy? Why?

What are the advantages of the participating policy?

On what theory are loans made by insurance companies?

CHAPTER VII

BUSINESS METHODS OF LIFE INSURANCE

1. *Loading.*—The expenses of the business of life insurance are provided for by an addition to the net premium, called a loading. The premium itself, as computed by the mortality tables and the assumed interest earnings, may be called a net or pure premium, and does not contain any provision whatever for expenses.

In other forms of insurance, as in fire, the cost is not covered by such an addition, but has always been considered as forming a part of the rate computation itself. The loading may vary for different policies and in different companies, but, as competition between the different companies is keen, the cost of insurance among the old-line companies is kept down. They must maintain a sufficient reserve at all times to meet their obligations, and competition is a fairly effective hold-back to any undue ambition to put the premium at too high a point by means of loading.

2. *Settlement of claims.*—In the older method of settling claims adopted by the Equitable of London which has already been described, some claimants were made to wait very nearly if not quite a year before they received the insurance fund. Under the present

method, expedition in the settlement of claims is a marked feature of the modern life insurance companies. Probably 95 per cent, if not a somewhat higher proportion, of claims are paid within forty-eight hours from the time the proofs of death are received at the home office.

The life insurance company furnishes certain forms which are used in the preparation of claims. One form, filled out by the claimant, sets forth the basis of the claim and gives evidence that the deceased person is the one that was insured under the policy. A statement of a physician, assuming there was one, who attended the insured in his last illness, is usually required. Another statement is made by the undertaker or it may be the clergyman, testifying to the fact that the person buried was the one described in the claim papers. There is often a statement of a friend as to the identity of the deceased and the circumstances of his death. Not all four of these statements or sets of papers, may be required in all companies, but these cover the usual run of the cases.

3. *Life insurance in its commercial aspect.*—Protection to the family, which was the primary idea in the beginning of life insurance, has lost none of its original force, and perhaps is more prominent today than ever. At the same time there is a tendency to look upon life insurance as a commercial undertaking and to disassociate it from the "You must die to win" sentiment. Life insurance is simply an investment for the purpose of prolonging the earning power of

the individual when the individual himself may have lost the power to continue earning. This is the common-sense view of the matter that will probably have the greatest influence in the upbuilding of the great business of life insurance.

There are, however, cases which perhaps come more closely within the realm of commercial life insurance. Some of these may be suggested: In New England a noted hotel keeper desired to erect another hotel and still continue the one in which he had earned his fame. In fact, at the time of this incident, he was managing successfully two important hotels in the city, but desired a third, which was to be run on somewhat different lines. His venture in the new hotel would represent an investment of something over a million dollars. Capitalists were willing to make the investment if there was a reasonable assurance that the hotel would be managed by this person. As part of the investment, they insured the life of the manager and so protected their venture. The hotel was built and successfully managed for many years. This is an incident of commercial insurance.

Many corporations find that their success will depend on the life of a certain individual if not thru a long period, at least thru the time, perhaps three, five or ten years, necessary to build up the business. The common-sense thing to do, which is being done every day, is to insure the life of that individual, and free both the individual and themselves from any strain incident to the fear that the whole thing would

come down in ruin thru the loss of this valuable and important life.

The extent to which this form of protection may be carried is almost unbelievable, and yet, new uses are being found for it almost daily. Many years ago the large jobbing and manufacturing interest decreed, and have continued so to decree, that those who purchased goods from them on credit must carry fire insurance. We fancy, the time is not far distant when similar parties will insist on life insurance being carried as an additional protection to the business in case the individual dies. In partnerships, in corporations, in a multitude of ways, this great principle of life insurance, which merely conserves the individual's efforts, is coming into play and is doing its great work.

4. *Group insurance.*—Until recently life insurance has been like the old method of picking berries, in that it has been done one at a time. It is now realized that a greater service to the community can be provided with absolute safety by insuring people in groups, and many policies are being issued, covering all the employes of a given enterprise. These group policies usually provide for payment in case of the death of an employe equivalent to one, two or three years' earnings, and it is quite needless to point out what that means to a family. The premiums on such policies are usually paid by the employers themselves. It is a business asset; it is a bit of welfare work; it has that about it which tends to make the relations between the employer and employe more satisfactory; all this, in

addition to the positive good to the family, should the death of the individual occur. The group policies do not require medical examination for the original group insured. Later additions to the group are usually subject to examination.

5. *Assessment insurance.*—In the beginning of life insurance, say not further back than 1762, when the old Equitable was founded, the premiums were the same for everybody who joined the society. The age limitations were quite well established and they were placed rather low, but it was some years after this before an accurate knowledge as to the workings of the law of mortality were not merely understood, but acted upon. In connection with matters of insurance, man has, almost from the beginning of life insurance, attempted in one way or another to buck the law of mortality. It is, of course, and always will be, a losing game. He may use the law quite to his advantage and adapt his practices in conformity therewith, but he cannot defy it successfully for any length of time.

Assessment insurance is said to have first appeared in the United States some sixty years ago, tho at that time it was probably in a somewhat small, tentative affair, having a fraternal origin, the benefits being small and confined to the members of certain lodges.

6. *United workmen.*—In 1868 there was founded at Meadville, Pa., by Father John Upchurch, the ancient order of United Workmen, a trade union, as a matter of fact, but as an incidental feature,

there was a requirement that there should be a contribution of one dollar, paid into a common fund, on the death of a member, which should go to his widow. The organization grew, not because of this feature, but because of the other elements in the plan; but its growth soon brought it to the point where the indications were that benefits of one thousand and two thousand dollars and even much larger sums would be paid under the one dollar contribution. The amendment was then introduced which fixed the maximum death benefit at two thousand dollars. This organization had a remarkable growth, with a membership at one time of about half a million in the United States and Canada. The success of this organization led to the founding of others having the characteristics of lodges, altho there were many other societies which did not use the lodge system.

Up to this time the furnishing of insurance on this plan was associated with organizations whose primary purpose was something else. Some of them became more interested in the death benefit feature than anything else and many were turned into what was known as business assessment organizations whose only purpose or excuse for living was to assess the members for the death benefit and pay it out to the beneficiary. Probably very few, if any, were founded on sound actuarial principles, and they passed away.

Life insurance in the United States up to at least 1870 was more or less experimental. The belief was general that the cost of life insurance was actually

much less than the life insurance companies charged for it. The question of the proper reserves was little understood, even among many engaged in the business.

7. *Mortality record.*—In the first five years of insured lives, there is and may reasonably be expected to be, and ought to be in fact, a much lower mortality record than exists among the population generally. When an assessment association begins, the assessment may for a while run fairly low but, in due course, there will be an increasing death rate among the members and the assessment must steadily increase if the promised benefits are to be paid. It is impossible to provide life insurance with a definite payment to the beneficiary except in two ways. One, to make the provision on the old line principle, which establishes under actuarial tables the proper charge to be made each year for the policy issued. The other way is to increase the payment as the insured life grows older. Unfortunately, of course, that is precisely the time of life when fewer persons are able to meet the increased obligations.

There has been compiled what is known as the National Fraternal Congress Table, based on the experience of the fraternal societies. The difficulty with this table is not a lack of accuracy, but that its introduction in any existing society means a higher rate of assessment. This results usually in a loss of the membership sufficient to cause the society to pass away or

8. *Fraternal insurance.*—Closely allied to the assessment form is fraternal insurance, tho greater emphasis is placed on other benefits to be derived from the association. Some fraternal orders have a membership of over a million and it is estimated that the total membership of the various fraternal societies is not far from eight million persons. Like the business assessment companies, they have had difficulty in placing their affairs on an actuarial basis because they started with the same fallacious ideas concerning the law of mortality. Yet these two forms of insurance have probably done a very large educational work in regard to the value of insurance. The income of these societies at the present time is approximately one hundred millions of dollars. The reserves carried are comparatively small because the principle of such organizations is that the money should be collected when needed and not piled up in the form of vast reserves. This sounds reasonable, but it bears heavily upon the members as they grow older. With increasing assessments the older members are too frequently obliged to drop out and give up their insurance just at the time of life when they most need it.

9. *Industrial life insurance.*—Insurance for the masses rather than for the classes, or the more carefully selected lives of the old-line companies is the claim of what is known as industrial life insurance. It is conducted on proper actuarial principles, but the very nature of the problem makes it necessary to de-

vise special means for transacting the business. This form of insurance appears to have originated in England in 1854, when the Prudential Assurance Company of London commenced to issue what is called industrial policies, in connection with the ordinary business of life insurance, which it was then transacting. To this company is due the credit for establishing this very important branch of business on the solid foundation which it now enjoys. Its importance in Great Britain can be appreciated when we recall that something like twenty million individuals are insured in the policies issued by this company.

10. *Industrial life insurance in the United States.*— In this country industrial life insurance is due to the late John F. Dryden of New Jersey. The first industrial policies were sold in the year 1875 in Newark, N. J. The company issuing them changed to the present name, The Prudential Insurance Co. of America in 1877. The principal companies engaged in the business are the Metropolitan, The John Hancock, Columbian, which, with the Prudential, transact probably not far from 90 per cent of this form of business in the United States, altho there are some twenty-five companies that issue such policies. Approximately seventy million lives thruout the world are now protected by policies of this kind, over twenty-four millions of these policies being in the United States.

What are the essential features of this form of insurance? (1) Policies are issued for small amounts,

ward, from that sum, to an infant life of not more than $10. (2) Premiums are multiples of five cents. (3) Premiums are payable weekly and are collected by the agent calling at the house. (4) Insurance is provided for the whole family.

Some of the methods of this form of insurance may be briefly noted. (1) If death occurs during the first six months of a policy, only one-half of the amount of insurance is usually paid; (2) there is a period of grace, the same as in the case of other policies; (3) the policies are usually incontestable one year after dates; (4) the policies may be converted in due course and at the proper age into ordinary policies; (5) there is the usual clause against naval and military occupation; (6) there is a cash surrender value as in the case of the ordinary policies; and (7) endowment policies as well as life policies are provided for.

11. *Industrial premiums.*—The premiums run from three cents, five, ten, fifteen, twenty, twenty-five, and so on. In one company the highest amount that can be insured for is $996 at the age of twenty-eight, the premium being sixty cents a week. At age ten, a weekly premium of five cents is charged, the amount payable if the policy has been six months in force, is $150. At age twenty the amount payable is $105. At age thirty it is $79. The companies now provide that if one attains the age of seventy-five the insurance is continued in force but the payment ceases. Regarding the future of industrial insurance Mr. Frederick L. Hoffman says:

Industrial insurance is now a thoroly well established method of family protection, intelligently adjusted to the needs and conditions of wage earners and their dependents. In the natural evolution of the business constant progress is being made and every year improved or new features are introduced into the policy contract, or in the relations of the companies to their policy holders, which shows the people that in years to come industrial insurance will serve a still larger social and economic purpose than at the present day.

REVIEW

Give some instances of the use of life insurance in business.

What is the most recent development in this field of insurance?

What are four characteristics of industrial insurance?

A holder of an industrial insurance policy joins the National Guard. What should he do to keep his policy effective?

What fact of mortality has often been left unprovided for by assessment companies?

What are the results?

CHAPTER VIII

CASUALTY INSURANCE

1. *Origin of casualty insurance.*—The general name given to the branches of insurance other than marine, fire and life, is Casualty Insurance. In the early part of the nineteenth century when branches other than the three big ones began to be developed, the name Accident Insurance was, altho it applied to a special branch, used for some time to designate these various additional forms of insurance. In due time, however, the phrase Accident Insurance was limited to its special phase, and the broader expression, Casualty Insurance, came into use, and is continued to the present day.

One of the most comprehensive lists showing the various forms of insurance of all kinds is put forth by the Brokers' Association of Great Britain. The long list which would be included under the terms casualty insurance is worthy of note:

ENGINES, BOILERS AND ELECTRIC PLANT:

Engines, Boilers and Electric Plant.

CASUALTY:

Coupon.

PERSONAL ACCIDENT:

Personal Accident.
Sickness and Accident.
Do. With Life Ass.
Do. (All Risks.)
Contract Guarantee.
Dentist's Indemnity.

Cycles.
Hailstorm.
Lifts and Cranes.
Live Stock.
Motor Cars.
Motor Cycles.
Plate Glass.
Third Party and Driving.
Transit.
Workmen's Compn.

VARIOUS:
Accountants' Indemnity.
Bad Debt and Credit.
Burglary.
Druggist's Indemnity.
Fidelity Guarantee.
Forged Transfers.
Keys.
Leasehold Redem.
Licenses.
Mortgage.
Patents (Infringement).
Property Owner's Ind.
Rail. Wagon Do.
Registered Post.
Solvency Guarantee.
Sprinkler Leakage.
Trusteeships.

2. *Extent of casualty insurance.*—The latest figures of casualty insurance, using the reports of the State of New York, are as follows:

(a) The assets were $203,000,000, which showed an increase over the preceding year of $17,000,000.

(b) The liabilities, not including the capital, were $123,000,000, while the total amount of capital was $46,000,000.

(c) The total income was $157,000,000. $141,000,000 of this amount was received from premiums.

(d) The disbursements were $141,000,000. The dividends to stockholders were approximately $5,000,000.

(e) As illustrating the somewhat close underwriting conditions of the business as a whole, it may be stated that there was a net loss from underwriting for the year of $820,000.

The relative income from the different branches in casualty insurance is reported as follows:

Personal Accident	$25,750,000
Health Insurance	6,750,000

Liability	$34,300,000
Workmen's Compensation	31,850,000
Fidelity and Surety	22,000,000
Plate Glass	4,700,000
Steam Boiler	3,000,000
Burglary and Theft	4,700,000
Automobile and Teams, Property Damage	5,500,000
Other classes	2,800,000

Insurance business other than fire or life was carried on in Canada during 1915 by 28 Canadian, 14 British and 35 United States companies. Thirty-seven of these companies likewise transacted fire insursurance, and one transacted life insurance. In addition to these 77 companies, there were 5 fraternal orders or societies which carried on sickness insurance and also life insurance.

Of these 28 Canadian companies which carried on business other than fire or life, 21 transacted miscellaneous classes of business only. Of these, 13 transacted sickness insurance; 12 accident insurance; 7 plate glass insurance; 8 guarantee insurance; 9 automobile insurance; 2 steam boiler insurance; 4 burglary insurance; 1 weather insurance; 1 hail insurance; 1 live stock insurance; and 1 title insurance.

The total amount of premiums received in Canada in 1915 for all forms of insurance, excluding fire and life insurance, was $8,133,483. The following summary shows the distribution of the premiums to the various classes:

Automobile (including fire risk)	$312,427
Automobile (excluding fire risk)	323,658

Personal Accident	$1,684,010
Combined Accident and Sickness	402,753
Guarantee	730,138
Plate Glass	269,263
Steam Boiler	150,377
Burglary	91,885
Sickness (so far as separate return made)	1,084,798
Inland Transportation	165,450
Employers' Liability	1,952,250
Sprinkler Leakage	38,781
Title	79
Live Stock	79,971
Hail, Weather and Tornado	841,694
Explosion	5,949
TOTAL	$8,133,483

3. *Scope of casualty insurance.*—The principle of insurance is capable of wide extension. It would be impossible to enumerate all possible cases in which insurance against a risk might properly be taken. One case in the English courts brought out a contract under which a man interested in a lecture tour of Miss Ellen Terry took out a policy, by the terms of which she was to receive £100 for each and every engagement, which thru sickness or any other cause Miss Terry was unable to keep. It appeared that this man had made himself responsible for all or a part of Miss Terry's traveling expenses, for which he was to receive a share in the profits of the tours. Under the terms of the insurance as construed by the court, the insured would have been entitled to an indemnity had he suffered any loss as a result of his contract with Miss Terry.

4. *Personal accident insurance.*—Among the very earliest branches of casualty insurance to be developed was personal accident insurance. In 1848 in Great Britain it was proposed to organize a company that should insure those taking railway journeys against injury on the journey. It is perhaps needless to point out that railway travel was then in its infancy, and that the idea of insuring those who might be injured on such journeys seemed but little short of madness. However, in 1849 the Railway Passenger Assurance Company was organized by a special act of Parliament. In 1852, finding that the insuring of persons traveling on railways would apparently furnish a limited field, the company obtained a charter amendment which enabled them to engage in accident insurance on more general lines. The adventure was successful from the beginning, and many other companies sprang into existence.

In connection with this form of insurance, it is exceedingly interesting to note that those who first planned the work were either so skilful or so fortunate as to adopt a series of charges which have furnished a basis for all future work of this kind. Many of the actual charges are still in use altho the benefits under them have been greatly extended.

5. *Accident insurance in the United States.*—It is to James G. Batterson that accident insurance in the United States owes a great deal of its success. Traveling in England, he purchased a railway accident ticket, and was impressed with the value of the idea.

On returning to the United States he sought, in 1863, and obtained a charter from the legislature of Connecticut. The Travelers Insurance Company had at first a somewhat limited field, but in 1864 the charter was amended and it was permitted to issue policies against all forms of accident. From this beginning the business has developed until at the present time some sixty-five companies on the stock plan—not to mention mutuals—are engaged in this form of insurance.

6. *What is an accident?*—In this form of insurance the question arose very early when claims were made as to whether the injury was caused by an "accident." It is evident that the difficulty, like most other questions, comes when the case is on the border-line, and the best way to present it is to give the opinion of the court in two or three cases:

In the case of the United States Mutual Accident Association vs. Barry (131 U. S. 100), the assured died from injuries sustained in jumping off a platform. The Supreme Court approved in its decision the following instructions:

> We understand from the testimony, without question, that the deceased jumped from the platform with his eyes open, for his own convenience, in the free exercise of his choice, and not from any perilous necessity. He encountered no obstacle in jumping, and he alighted on the ground in an erect posture. So far we proceed without difficulty. But you must go further and inquire, and here is the precise point on which the question turns: Was there or was there

not any unexpected or unforeseen or involuntary movement of the body, from the time Dr. Barry left the platform until he reached the ground, or in the act of alighting? Did he or did he not alight on the ground just as he intended to do? Did he accomplish just what he intended to do, in the way he intended to? Did he or did he not unexpectedly lose or relax his self-control in his downward movement? Did his feet strike the ground as he intended or expected, or did they not? Did he or did he not miscalculate the distance, and was there or was there not any involuntary turning of the body in the downward movement, or in the act of alighting on the ground? These are points directly pertinent to the question in hand.

And I instruct you that if Dr. Barry jumped from the platform and alighted on the ground in the way he intended to do, and nothing unforeseen, unexpected, or involuntary occurred changing or affecting the downward movement of his body as he expected or would naturally expect such a movement to be made, or causing him to strike the ground in any different way or position from that which he anticipated or would naturally anticipate, then any resulting injury was not effected through any accidental means. But if, in jumping or alighting on the ground, there occurred, from any cause, any unforeseen or involuntary movement, turn, or strain of the body which brought about the alleged injury, or if there occurred any unforeseen circumstance which interfered with or changed such a downward movement as he expected to make, or as it would be natural to expect to make under such circumstances, and as caused him to alight on the ground in a different position or way from that which he intended or expected, and injury thereby resulted, then the injury would be attributable to accidental means.

In what are called the poison cases, an injurious substance was taken by mistake. In the case of Riley vs. Interstate Business Men's Accident Association

(152 N. W. 617), the chief justice spoke thus on the matter:

I am entirely clear that John N. Riley came to his death by external, violent and accidental means, and am just as certain that deceased did not voluntarily take poison. The only question in the case to my mind is, Did he take it involuntarily, bringing its taking within the meaning of the exception in the policy? The question is a narrow one. What is the meaning of the term "involuntary taking of poison"? I confess to some doubt on this proposition, for I hesitate to apply it so broadly as to cover every case of unintentional poisoning, as where it results from some lethal substance found in ordinary food, or any case where the poison is inadvertently mixed with other apparently innocuous substance or substances by accident only.

There is some reason for saying that the exception is no stronger than if it had read that the policy should not be held to cover death from the taking of poison, no matter whether the assured was sane or insane at the time of its taking. But on the whole I am disposed to think that it is broad enough to cover death resulting from the voluntary or involuntary taking of poison, provided the poison be of the kind generally regarded as such, that is to say, arsenic, strychnine, carbolic or sulphuric acid, or other drugs commonly known as a poison as distinguished from a drug, or other concoction which, although poisonous, is not generally recognized as such. I wish to so limit my concurrence so that ptomaine or other like poisoning, the taking of an overdose of medicine not generally regarded as a poison, or any other case except one where death directly results from the voluntary or involuntary taking of what the ordinary mind regards as poison, is covered by the policy.

7. *Scope and development of personal accident insurance.*—In personal accident insurance, for a given sum and other considerations the company agrees to

pay to the beneficiaries, if the insured be killed by accident, a fixed sum of money; or if the insured be injured there will be paid to him either a stipulated indemnity for the loss of an important member, as an eye, or a stipulated indemnity per week for the time the injury lasts; but not, of course, in any case would the amount paid exceed the face amount of the policy.

The records of accident insurance show very clearly the rise and decline of the popularity of the bicycle. Since the automobile has come into existence an enormous increase in the business and in the claim costs has occurred. Statistics show that 25 per cent of all the accidents for which benefits are paid occur at home. Another 20 per cent occurred to pedestrians. Automobiles represent 10 per cent, and ordinary forms of recreation the same. At one time the number of accidents caused by automobiles and horse-drawn vehicles respectively was about the same, but the rapid increase in the number of automobiles is making accidents from this source far more numerous than those caused by the horse-drawn vehicles.

8. *Premium.*—The basis of accident policies is so much for each thousand dollars of indemnity; ordinarily it is five dollars. Probably the most popular policy is the one which is twenty-five dollars a year for five thousand dollars, at death, with proportionate benefits for injuries which do not result fatally. These benefits and price have undergone some change,

but the most important changes have increased the benefits rather than modified the charge.

One of the features early introduced was a certain percentage of increase in the benefits, usually 10 per cent, for each year up to five after the first time the policy was renewed. Thus, a person who had been insured five years, secured for the same sum of money, benefits of seventy-five hundred dollars under the five thousand dollar policy. Another feature was the doubling of the benefits when death was caused under certain circumstances, as in a burning building, on a railroad train or in an elevator.

That such double benefits are of more than ordinary moment may be illustrated by the case of a noted architect in New York City. Upon leaving a friend's house, where he had been visiting, he called a taxicab, in which he rode from the side street to the avenue. A short distance from his friend's house it collided with a trolley car. The cab was upset and the architect so badly injured that he did not recover. His accident policy was for twenty-five thousand dollars, and subject to double benefit for an injury which happened in this manner, and, as it had been in force for a couple of years, the 10 per cent increase made the payment somewhat larger than twice twenty-five thousand dollars.

Accident insurance, like life insurance has been subjected to all the schemes and strategems of those who seek to defraud, and much wisdom has been required on the part of physicians and those who settle claims

on losses to detect such plans. It seems incredible that one would purposely injure himself even to the extent of parting with an important member of the body for the purpose of obtaining funds from accident insurance, but actual cases show that this has been done.

9. *Automobile insurance.*—It would appear from the record that the Boston Insurance Company was the first concern to offer policies of insurance against a series of hazards to which the automobile and its owner are subject. Naturally, the machine had always been insured against fire by the regular fire policy; but broader insurance was required by the development of the machine, and that came into existence. At first its broader coverage was limited to insurance companies devoted to the casualty business; but many of the fire insurance companies have been granted the privilege of engaging in this form of insurance.

Automobile insurance covers:

1. Fire or explosion
2. Transportation, i.e., derailment and collision
3. Theft
4. Damage by fire to personal effects carried upon the car
5. Damage to other property by being in collision with the automobile insured—known as property damage
6. Damage to the automobile insured by being in collision with some other object
7. Loss of life or injury to the occupants of the car and legal liability for expenses in connection therewith
8. Loss of life or injury to others and legal liability for expenses in connection therewith.

When one considers this list of hazards, it is evident that the charge must be proportionate to the risk assumed. It must be borne in mind, however, that the use of these vehicles is equivalent to permitting steam engines to run on the streets. We should at once recognize that a high rate of insurance would be required to cover such a hazard. An examination of the daily papers shows the steady toll in the loss of lives, machines, and injury in other forms, which must be allowed for in this type of insurance.

10. *Plate glass insurance.*—The breakable nature of glass might alone seem enough to prevent the development of an insurance company to take care of this risk. Plate glass insurance is now, however, a very substantial business. It originated in this country in 1868, when the New Jersey Plate Glass Insurance Company was organized. When only small panes of glass were manufactured there was but little demand for this type of insurance, but as the demand came for large pieces of plate glass and the value of a single pane increased, some form of protection became a necessity. The growth of the business may be ascertained by comparing the premiums in 1874, which were $18,000, with those of today, which amount to $5,000,000.

It is estimated that there are at least 400,000 store fronts insured under plate glass policies. The business differs from possibly all others in that most of the losses are not settled by cash payments. The company replaces the glass, and for this purpose main-

tains warehouses at central points, or makes arrangements with jobbers for handling the losses.

The causes of breakage number about one hundred. Stones and the small boy are accountable for about 75 per cent of all the losses. There are certain mechanical features, such as the settling of a building, which may cause a loss; or the glass itself may be improperly set in the sash and the undue strain may cause it to break.

The cost of replacement varies. In the metropolitan centers the contracts with the jobbers can be made to fair advantage and even large losses can be quickly replaced; but away from the larger centers, especially if the glass is of unusual size, the cost runs up to comparatively large figures. This cost of replacement naturally is a very important matter to take into consideration in writing the insurance.

The risks assumed cover also the show-cases in stores. These are often damaged by objects placed on them for display. Church windows are in a special class. If the window, as is quite likely, was made in one of the large cities, but placed in a church in a distant part of the country, the cost and expense are duly increased accordingly. The windows above the first floor are seldom insured, since they are considered outside of the zone of danger. This view, however, has changed since the noted explosion and fire in July, 1916, at Black Tom Island in New York Harbor. The loss was the largest from a single disaster in the history of the plate glass insur-

ance business, and incidentally it gave the business an amount of advertising which it perhaps could not possibly have received in any other way.

The fact that so fragile a thing as glass can be successfully insured reveals the possibilities in the field of insurance for many types of risks which are now considered outside the scope of that business.

REVIEW

To what risk was casualty insurance first applied?

A person, while asleep, is killed by breathing escaping gas. Would the death be covered by casualty insurance?

Enumerate ten different forms of death by accident that may be covered by casualty insurance.

X takes out insurance on his automobile. Subsequently he runs over Y, who brings suit against him. By whom is X's case conducted?

Trace the development of accident insurance in the United States.

CHAPTER IX

CASUALTY INSURANCE (*Continued*)

1. *Steam boiler and fly-wheel insurance.*—The development of steam boiler insurance was the logical thing when the risk had reached the point where sufficient information in regard to it had been gathered so that insurance could be brought to bear upon it. This form of insurance, like that of personal accident insurance in connection with railroad travel, was among the earliest of the casualty lines to be developed. It has now passed its fiftieth anniversary, while its younger cousin, fly-wheel insurance, was not taken up until 1901.

The distinguishing feature of these two forms of insurance is conservation. The funds gathered in the form of premiums are not spent primarily—and are not intended to be—for the payment of losses, altho those are, of course, paid; but a larger proportion of the funds, perhaps, than in any other branch of insurance is expended in the high-grade inspection service which it is necessary to maintain if this business is to be carried to a successful conclusion.

No money indemnity can pay for the loss of a life, and that usually results when a boiler explodes. It is found that one boiler in every 170 is mechanically

defective and physically unsound, so that it is not safe to operate it and, naturally, is not insurable. One boiler in seven has defects that require attention, and sometimes the immediate suspension of work; while one boiler in every two possesses some defect, altho it may be of a minor character. One boiler in three has scale, and one in every seventy is affected by it to a dangerous degree. The insecure stay-bolt is found in one of every sixty boilers; while one in 270 is positively dangerous on account of this defect. A fractured plate or head is found in one boiler in forty, and one in every 250 is seriously affected. One man is injured annually, to every 1,000 boilers under steam; and one killed, to every 5,000 boilers in operation.

This list of defects and disasters could be expanded, but as it stands it is sufficient to put one in touch with the general conditions which inspection service has shown in this important field of conservation. All too frequently the insured does not appreciate the loss that will follow from the shutting down of his plant. The failure to make allowance for such loss is too often the reason why the insured is indifferent to the kind of insurance which brings him inspection service.

Fly-wheel insurance, which is now in its seventeenth year, is a very small part of this form of insurance; its total premiums amount to only about $250,000 per year. Undoubtedly the increasing use of electricity as a form of light, heat and power has had a marked effect on the development of steam power.

There does not, however, seem to be any reason for supposing that steam power will entirely pass away in the near future.

2. *Hail insurance.*—Loss from damage inflicted by hail upon growing crops is often provided against by hail insurance. It was developed on the continent of Europe many years before it was introduced into the United States. At first it was very largely a mutual affair. Stock companies did not enter into the business very largely before 1910; the last two years have proved so unfavorable that many of them are already retiring from it. In one of the states this form of insurance is undertaken by the state, which takes charge of the transaction, collects the funds and distributes the payment for losses. The experience in that state has not been satisfactory, since the rates fixed have allowed only a partial return to those insured for the losses which occurred.

Late in April in the southern territory of the United States the writing of hail insurance begins. It moves northward as the season advances and stops in the Canadian provinces of Saskatchewan and Alberta in the month of July. All of the policies expire on September 15th, irrespective of the date on which the policies are written; but if the grain is cut earlier than that, liability ceases from the time it is harvested.

Of all growing crops cotton is said to be the most hazardous. Tobacco also ranks as hazardous, because of the broad leaf's susceptibility to damage

from hailstones. Altitude has a bearing on the matter; the grain fields of Colorado are written at a loss, altho the rate may be four times that in the lower sections.

The question of moral hazard is an acute one in this business. This can be readily understood if one realizes how a small rain or hail storm might be considered as causing all the damage to a growing crop, altho the growing crop itself might be quite substandard.

3. *Central organization.*—The settlement of hail losses has not been reduced to a scientific basis in any sense of the term. Perhaps the lack of success of the stock companies is due largely to this fact. Before they had formed a central organization, the companies were quite at the mercy of the insured. The central bureau, however, has accomplished a vast amount of good work in this field of insurance. It is as important to the insured, as a body, that the losses be equitably settled as it is to the individual. Those who do not suffer a loss may be said, after all, to be those who are paying those who do, and anything that unduly increases the losses unduly increases the charge that must be made. This fact, with a foundation in equity, is a paramount consideration in dealing with the whole question of central organization for handling property insurance.

Mr. Walter C. Leach, president of the Western Hail Association, thus set forth the requirements for an adjuster:

The adjuster must be a man of strong physique, capable of tramping the field all day, and between times doing 100 miles or so in a Ford every twenty-four hours; be prepared to be bitten by the bull-dog when he lands on the premises, and to drive off under cover of a shotgun if his settlement is not satisfactory. He must speak not less than three languages, swear in none, and have a temperament that is under absolute control at all times—in fact, it is a heart-breaking job requiring a combination of physique, knowledge and diplomacy that is not easy to find.

Over 35,000 claims were handled by the association during the past year. It is a form of business which has been quite lucrative to the insurance agent. At first the premiums were paid in cash, but later the note system was introduced. As competition, when too keen, tends to break down sound standards, an undue extension of the note system has probably crept into the business. But this all bids fair to be taken care of by the central organization as soon as it has had a few years more of experience on which to base better practices.

4. *Hail insurance in Canada.*—Hail insurance in western Canada has for some years past been written by (1) municipalities organized by the provincial government; (2) mutual companies; (3) joint stock companies. The importance of carrying hail insurance was particularly impressed upon the farmers of the provinces of the Dominion in 1916. In the history of agricultural Canada there had never been so disastrous a season as in that year. Probably over 10 per cent of the entire crop was destroyed by hail.

The only protection against hail is furnished by an insurance policy placed with a reputable underwriting organization. No care or forethought will minimize the possibility of disaster as it may in the case of fire risk. In Saskatchewan, a municipal hail insurance commission has been created. It has inaugurated a system of cooperative, or mutual insurance, whereby a farmer whose crop is situated in a rural municipality may procure insurance, under the hail insurance act, to the extent of $5 per acre in addition to the $5 provided for by an assessment of 4 cents per acre made by municipalities that have passed a prescribed hail insurance law.

Agents have been appointed to solicit business for the commission in about 150 rural municipalities. The commission completed arrangements with several good companies whereby a portion of the risk could be reinsured if the amount of insurance applied for was greater than it was considered safe to carry. This arrangement has been carried out in a number of districts, in fact, wherever it was considered that there was even a slight risk of overloading, while in other districts where the lands of farmers taking this additional insurance were more isolated and scattered it was not considered necessary to effect reinsurance.

The rate charged for the additional hail insurance is 5 cents per acre for each dollar of insurance, which is 1 per cent per acre less than is usually charged, but the commission calculated that as its administration expenses were low, the deficiency in revenue

caused by the reduction of 1 per cent in the rates would be easily made up.

The unfavorable experience of 1916, however, upset calculations. The Saskatchewan Hail Insurance Commission's losses in that year were approximately $3,500,000. The available assets of the Commission, including the current revenue and surplus from the previous year, amounted to $1,500,000, while the losses thruout the system were more than double that amount. So that 50 per cent was the highest amount the Commission could pay on claims.

While the hail losses in the year under review had more than taxed the capital, this fact did not, in the opinion of the chairman of the Commission, show any fault in the system. He was inclined to the opinion that it simply went to show the necessity for establishing a good security for hail insurance and for building up a large surplus. He advocated an all-round increase in rates, stating that such action was imperative. A 4-cent flat rate should, he suggested, be maintained, under the insurance act, on all lands, but this rate should carry $5 per acre on land up to 80 acres only on a quarter section, and a graduating scale of 1 cent per acre should be added on the whole quarter section for each additional 20 acres, or portion thereof, under cultivation. This would mean a flat rate of 8 cents per acre if a full quarter section were under cultivation. It was proposed that if there are 100 acres under cultivation on a quarter section the rate should be 5 cents; if there are up to 120 acres the rate should

be 6 cents; if there are 140 acres the rate should be 7 cents; and if an entire quarter section is under cultivation the rate should be 8 cents per acre.

The experience of the Saskatchewan Commission lends emphasis to the statement on a preceding page that the settlement of hail losses has not been reduced to a scientific basis; and in Canada it is apparent that rate-making also is in an experimental stage.

Continuing with the Saskatchewan province in 1916 as our example, the 22 companies writing business also lost heavily. Their loss ratio averaged 132 per cent of the premium income. When to this percentage is added the underwriting expense, which covers commissions, adjustments and general office expenditure and which averages 30 per cent, it will be seen at a glance how disastrous for the stock companies was the hail season of 1916. In short, the companies not only paid out the total amount of money received by way of premiums, but they also paid from their reserves an additional amount equal to 62 per cent of the 1916 premium income.

At the same time, they paid their losses in full. The mutual and stock companies are required by law to make large deposits by the governments by which they are licensed or registered. In addition, they have to pay taxes and should they not pay their policyholders 100 cents on the dollar, their licenses are liable to cancellation by the governments concerned. Ten per cent would not have been an adequate premium in 1916, for the Saskatchewan gov-

ernment Commission to charge. The stock companies which charged approximately 6 per cent were able to draw on their assets and pay the farmer the full amount of his loss within a few days after the storm. On the other hand, the municipal insurance Commissions were able to pay the farmer only 40 or 50 cents which their funds allowed them to pay, and some difficulty was experienced in doing that.

The government must accept every risk offered them, while a well-managed company would not take one-half of the business of ten adjoining townships, even if they could get it. It is obvious, therefore, that important changes must be made in the conduct of the business in western Canada, particularly in regard to the operations of the government Commissions.

5. *Burglary insurance.*—Protection thru insurance against loss by burglary originated in the United States in Reading, Pennsylvania, some time prior to 1892, but had no great development. In 1892 one of the larger casualty companies undertook to guarantee banks and bankers, and other users of safes, against loss of money and securities and other valuable articles thru attacks by burglars. The business had a very slow growth, and its upbuilding was not a matter of months, but of years. The bankers required much education. Some of this education took the form of advertising, and even demonstrations of how easy it was to break into a safe.

In 1895 the business amounted to about $65,000 a

year, and included only the banks in the small towns. Other companies entered the field in 1896, and from that period on, due probably to advertising, the business commenced to grow and has now attained a point where the income is almost $5,000,000.

The phrase "burglary insurance" means loss by burglars, and in the beginning the policies were somewhat restricted and covered what were known as safe burglars and bank burglars; but today the scope is broadened. In addition to protecting banks and trust companies, the business has been extended to protect the merchants, and also, of course, to protect the private homes.

6. *Other forms.*—The broadening of its lines, while it increased the business, brought certain problems; for instance, in the case of resident theft insurance there is difficulty in the adjustment of those losses which are due to disappearance. The articles have disappeared but it is impossible for anyone to state that they have been actually stolen. It is not difficult to prove a burglary because that usually means the entrance into the property, and there will in most cases be some visible mark; but this is wholly lacking in the disappearance cases. The policies now cover the loss from the person of jewelry and other ornaments. This is merely an illustration of the broadening-out process.

"Mercantile Open Stock Insurance" provides for stocks which are not protected by safes or vaults. These command a high premium because there is no

coinsurance and the experience with it has been rather unsatisfactory.

7. *Robbery insurance.*—Robbery insurance is analogous. It includes:

(a) Interior Robbery, which covers a hold-up in an office or store;

(b) Outside Messenger Robbery, which protects bank messengers, delivery men and collectors while away from their respective places, that is, engaged in some outside delivery;

(c) Payroll Robbery Insurance. The papers frequently announce that the employe of an institution returning from the bank with the money for the payroll has been held up and robbed. Some noted cases have occurred in this form of robbery, and protection is provided against it under the Burglary policies.

In this form of insurance there are six basic safe rates and ten basic vault rates, including many combinations, as, where the safe may be inside the vault. The rates are different for different territories, and there are allowances which depend on the size of the city or town, and discounts for burglar alarm and any watchman service. In robbery insurance the base rates are discounted for the number of guards who accompany the messenger, and for any additional safeguards deemed of value that are placed around the risk.

Those engaged in this form of insurance maintain a central organization for the purpose of standardiz-

ing many features of the business which are of common value, and probably this cooperative method has done as much as anything else to place a business—which by its very nature is precarious—on a sound and substantial footing. It is a business which in due time will grow, and if the principle of coinsurance can be introduced into the policies successfully it probably would mean a very widened scope for the business because the rates would be very much lower.

8. *Title insurance.*—Another form of insurance which merits attention is title insurance. It had its origin in the city of Philadelphia in the centennial year 1876. Its underlying idea was not so much to pay losses that occurred thru defective titles, but to change the method of passing real estate from one party to another. The plan contemplated was that instead of having the title examined individually, at every transfer of property, it would be possible to have it thoroly examined by competent parties, and that policies of insurance could then be issued against any loss that might occur because the opinion that the title was sound proved incorrect.

There is no real risk assumed here unless the work of searching the title by the company originally was defective, but the expense of the work is very heavy. It must be done by men of great ability, who command a good price for their services.

When first launched the business had to overcome the opposition of those who had done the work in the past, and also the general feeling that the examination

of the title was a thing that ought to be done whenever property was transferred. This hostile attitude has passed away, and title insurance has taken its permanent place in the world of business.

There are no renewal fees required in order that the policy may be kept in force. This is contrary to other forms of insurance, but the initial payment protects the title and covers the expense in connection therewith.

9. *Fidelity insurance.*—It was apparently about 1879 that bonds which guaranteed the honesty of a person began to be written. Like many names in insurance the designation is a bit misleading, since one cannot guarantee that a person will be honest; but what they can do is to give a bond which may be called upon for an indemnification should the person fail to be honest.

The business falls into three divisions: (a) the private employer; (b) Organization bonds, as they may be termed, states, counties and municipalities; and (c) those in favor of the United States government.

The first class of business—that for the private employers—is deemed of most value and most desirable. In considering the application for a bond on a specific individual the past history of the individual must be taken into consideration, as well as the opportunity or the temptation, which his present position offers. It does not follow that because the opportunity for taking funds may be large—as in that of a bank—that it is so. The opportunity may be quite counteracted

by the care which is exercised over the kind of property with which the employe is intrusted.

This statement is made with full knowledge of the fact that losses resulting from a failure to perform one's duty properly are almost a daily news item. But it should be remembered if it was not so rare it would not be a news item, and would fail to be recorded, and that there are thousands of banks.

Of course a company will lose at times by bonding a person who has secured a bond under an assumed name. His past record, if investigated, would have shown that a loss had already been paid by another company.

The public official has one element in his favor, the office which he holds—assuming he is a treasurer of public funds—is more or less of a public institution, and his work may be said to be conducted under the public eye. We know all too well that this is not always a fact, but nevertheless it is a consideration and is of influence in issuing a fidelity bond.

10. *Three classes of fidelity bonds.*—Fidelity bonds may be classified under three heads: (1) bonds issued for larceny or embezzlement; (2) the culpable negligence bond; (3) bonds issued for the faithful performance of duty.

In the first class, it is essential that the employer of the bonded person prove that his loss is caused by an act of dishonesty on the part of the employe, which comes within the scope of larceny or embezzlement.

The second class calls upon the employer to prove

that there has been culpable negligence on the part of the bonded person. Should the employe fail to return to the strong box important papers or money which had been taken out for examination, he would be deemed guilty of negligence, but not of any criminal offense such as larceny and embezzlement. It is evident that this phrase is capable of various interpretations, and comparatively speaking many cases go to the courts for the express purpose of settling the question as to whether or not, under the given circumstances, there was negligence which amounted to culpability on the part of the employe.

The third class of bonds, which guarantee the faithful performance of the duties of an official, has obviously a wider range than the other two. The range of duties may be so varied that the burden assumed is exceedingly large. One person may be responsible for the custody of the entire funds, or the responsibility may be divided; in many cases one person collects, hands over the proceeds to another, and the funds are paid out only on the order of a third party. There has grown up, in connection with this form of insurance, a method of issuing such bonds without the knowledge of the employe.

There are many cases where the employer may deem it prudent to bond an employe, altho it has never been done before; and owing to the long service of the employe, and so far as he knows, faithful service, he may not wish to wound his feelings by taking out the usual fidelity bond. The fidelity policy, as it has been

termed, may be secured in such cases. Naturally it commands a somewhat higher premium because the risk is somewhat greater, since it is in some degree, the insuring of a risk without an inspection of it.

11. *Surety insurance.*—The practice of becoming surety for another would appear to be, from Biblical references and other ancient works, one of the oldest commercial practices that is known. The bonds issued may be roughly classified as those of contract; of court; and of depository. There are also many other types, excise, forgery, customs, internal revenue and others.

The first, or contract bond, is one given for the faithful performance of a contract which a party has entered upon. These bonds are subdivided into three classes: (1) those for the proper performance of the work; (2) those for the furnishing of proper material for work; and (3) those for maintaining the work in proper condition after it is completed. In the performance of most contracts of this kind, the person for whom the work is being done usually retains a percentage of the payment to guarantee the faithful performance or the completion of the contract. Ten per cent is not an uncommon amount to hold back, and in some cases it is put at a higher sum.

All such forms of surety bonds should be examined with the greatest of care. The questions involve not merely the honesty and ability of the person who has the contract, but also the nature of the work to be per-

formed, the time limit, if any, and the past record of the contractor.

The practice of subletting many contracts must also be carefully considered, since the liability of the surety company runs out to many of these sub-contractors. Provision should, at all times, be made that the sub-contractor shall furnish a bond for his part of the work similar to that furnished by the contractor himself.

The second type of bond which guarantees that proper materials will be furnished has less risk since a fairly correct idea can be formed as to the price at which these articles must be purchased and sold in order to yield a profit.

The type of bond known as the maintenance bond has normally a limit of five years, but in some cases may be written for longer periods. Such bonds are generally issued to cover the up-keep of a road-bed, for the stated number of years.

In the case of bonds issued for court purposes there are two classes: (1) the fiduciary, and (2) the bond which is given by one party to a litigation which will enable him to follow out a legal remedy.

12. *Agreements in the bond.*—In the first class of bonds, the person who secures the bond enters into a stipulation for the faithful performance of his duties, and the company signs the bond as a surety, thereby making the guarantee of the conditions of the bond. Such bonds come into use in the case of the settlement of estates, in the case of guardians and trustees.

Where there is property the company that issues the bond being a party to the trust, has a good deal of control over the situation, since the funds cannot be tampered with without its knowledge, consent or signature. It will be evident, however, that having entered upon such a bond, the company must follow it out to the end. This requires steadfast watching which must not relax while the bond is in existence.

Depository bonds are those which are given for the purpose of guaranteeing that there shall be a prompt repaying of funds which have been deposited with banks. They are required by states, municipalities, counties, and a great many persons holding public positions. The desirability of such bonds depends on the conditions of the money market and business generally.

A bond which guarantees against forgery while quite an old type of bond in Great Britain, is rather new in the United States. Such bonds are used by banks as a protection against loss thru the forgery of checks or drafts.

REVIEW

In what form of insurance is the technical element of risk not found?

In what form of insurance are premiums devoted primarily to a purpose other than the payment of losses?

In what form of insurance is the moral hazard a vital factor?

Name three classes of fidelity bonds.

What types of bonds are found in legal proceedings?

What is a maintenance bond?

CHAPTER X

EMPLOYERS' LIABILITY INSURANCE AND WORKMEN'S COMPENSATION

1. *Rise of new phases of insurance.*—Legislation during the past thirty years in Europe has brought about to some extent in the United States, a new form of insurance to which the general title "social insurance" is given. In the United States the field of such legislation has been for the most part confined to questions concerning injuries which grow out of the accidents of daily employments.

The liability of the employer for the results of accidents is an old established principle of law, but under common law, both in Great Britain and the United States, so many exceptions were permitted, that it was difficult to secure redress for the injured employe. Space is lacking to give the successive steps by which the obstacles confronting the claimant were removed, and by which the responsibility in accident cases was fixed more definitely and irrevocably upon the employer. We are concerned with the development of certain types of insurance.

2. *Employers' liability insurance.*—The simple fact that under the common law most of the cases were obliged to be proved in the court by the plaintiff operated to limit the right of recovery, especially as the

cases did not usually come to trial for two years. This position of the employer was much improved by the adoption of a series of laws known as Employers' Liability Laws. These were based on two principles: (a) that the person who is guilty of negligence should be held liable for compensation to the injured person; and (b) the liability might arise not only from the deliberate act of negligence of the employer himself, but from that of his other employes.

3. *Employers' liability laws in United States.*—In the United States, employers' liability acts appear to have been passed in Alabama in 1885, Massachusetts in 1887, Colorado, 1893, Indiana, 1893, and New York in 1902. There were, as could be expected, some differences in the different states, but these were slight. The basic principles are the same in all cases. These measures were employers' liability laws with very distinct limitations as to the recompense which the employe might receive. None the less these acts placed greater liability on the employers, who began to take out insurance to cover such liability.

4. *Kinds of liability insurance.*—Besides employers' liability many other forms of liability policies were soon placed on the market. These may be briefly summarized as follows:

(a) The Public Liability policy which provides insurance against the liability of an employer to persons who are not in his direct employ but who may visit his plant legitimately, that is, are not trespassers.

(b) The Employers' Liability for Contractors. This protected the contractor against the liability which he assumed in employing labor on work in various parts of the country, that is, not limited to one location.

(c) Public Liability for Contractors, taking care for the contractor of persons legitimately on his place of business.

(d) General Liability, which provides protection to the owner of a building for injuries or death caused by defects about the building or its operation.

(e) Elevator Liability. This is for accidents caused by elevators.

(f) Team Liability, which provides indemnity to the owner for the liability which he may incur by reason of accidents caused by his vehicles.

(g) Theater Liability, which protects the management for accidents which may happen to persons in the theater.

(h) Vessel Liability, which provides protection for the owners of vessels.

(i) Physician's Liability, which protects the physician, surgeon or dentist, for liability for injuries which he may cause by errors in practice.

The growth of the business may be indicated by the fact that in 1887, the first year that policies covering liability insurance were written in the United States, the premiums were $131,000; while in the year 1915 they amounted to $22,000,000.

In all forms of liability insurance there is a com-

mon basis. In employers' liability contracts, it is an agreement to indemnify or make good to the insured any loss arising from the liability *imposed by law* upon the insured person for damages on account of bodily injuries or death suffered by any employe or employes of the insured, in the factory, shop, yard or other described place. In the case of the other policies, there is the same provision for indemnification for injuries arising to persons who, of course, may not be employes, but who may have been injured by elevators, teams, etc., belonging to the insured.

5. *Premium.*—The premium is based on the wages of the employes who are protected by the policy. The sums to be paid are usually fixed by the liability acts, and bear some relation to the earnings of the employes. These, therefore, furnish the basis on which the premium is based. It is not unusual to omit the salaries of the higher paid employes, as superintendents, foremen, etc., and this is usually acceptable to the insuring office because the large salaries which they receive in many cases would be a heavy liability to assume. In a large plant, or a small one for that matter, if the risks vary in different parts, the payroll for each division of course is taken into separate consideration, and a higher rate of premium may be charged for certain departments than is charged for others. The following quotation from the Yale Readings in Insurance, illustrates how rates may differ:

The rate for woolen mills, including employes and the public is .23 for each $100 of payroll. The premium for a

mill employing 500 operatives, old and young, skilled and unskilled, at average wages of $450 a year, would be $517.50, and the cost of the insurance per capita is $1.035. The rate for steel bridge construction is $9.00 for each $100 payroll. A structure furnishing employment to 500 men of all grades, at average wages of $700 a year, would require a premium of $3,150 or $6.30 per man.

6. *Reserves.*—The fact that a liability may develop long after the accident has occurred, and that the liability itself may be of uncertain amount, has made the problem of providing the proper reserves very difficult. It has been necessary to adopt, from time to time, additional safeguards against the reserve becoming inadequate.

In fire insurance, the losses are very rarely underestimated, but the liability insurance business is new and no general rules can be stated. The tendency has been perhaps to underestimate the losses. If they were correctly estimated, changes in the laws which increase the benefits, or the attitude of the jury which increases its awards, have been rather disconcerting and additional reserves have had to be provided.

This form of insurance does not concern property which can be properly appraised, but injuries to human beings, the appraisal of which must vary in different parts of the country, in different tribunals and with different individuals.

In general, the reserves are based upon the number of suits or settlements that have been taken care of in a past period, as from three to five years. The average cost of these furnishes a fairly accurate measure,

but like everything else it is, for the reason stated above, subject to readjustment at different times.

Employers' liability insurance, with the growth of social consciousness, is disappearing and giving place to what is called "workmen's compensation," but the other forms of liability and some parts of employer's liability, remain and still furnish considerable casualty premium income, and will probably continue to do so. The development of workmen's compensation out of employers' liability, is one of the most interesting features of the growth of civilization.

7. *Workmen's compensation.*—The difference between employer's liability and workmen's compensation can perhaps be grasped by the statement, that under employers' liability about one injury in eight which happened to an employe whose work came within the scope of the act, received compensation, and under workmen's compensation eight such injuries are taken care of.

A fundamental difference is that employer's liability took a merely legal view of the matter. It said, in effect, under the law the employer is legally bound to do certain things for his employes. Should he fail to do these a fixed responsibility rests upon him, which responsibility means a money payment. Workmen's compensation embodies the view that accidents and injuries which occur in connection with various business operations are, and should be considered, as a part of the cost of conducting the business. They should be paid for, just as the manufacturer would

pay for raw material which he might purchase for the purpose of converting it into another product.

8. *Workmen's compensation laws in the United States.*— In the year 1910, the legislature of the State of New York passed what is generally considered the first general workmen's compensation law in this country. In 1911, in the case of Ives vs. South Buffalo Railway Co., 201 N. Y. 271, the Court of Appeals declared the law unconstitutional. This was the first case to come before a higher court in the United States, in which the modern view of workmen's compensation was passed upon.

It became necessary to adopt a constitutional amendment in the State of New York, and it was not until 1913 that the present law went on the statute books. This law has been attacked in two cases, but has been sustained by the Court of Appeals in both.

The movement for workmen's compensation had received such impetus when the New York statute was passed in 1910 that, without waiting for a test in any one state, many of the states passed compensation laws. Seldom in the history of such beneficent legislation has the movement been so widespread in so short a period of time.

9. *State laws.*—The present status of these laws may be summarized as follows:

Thirty-two states and three territories have such laws in force, while Congress has passed a Federal compensation law designed to cover employes of the United States government and the Panama Railroad.

T law is optional, or, as it is often termed, elect-
i n fourteen of the states and two territories as to
1 classes of employers. This, in other words, means that in these states and territories the law is not compulsory upon any employer.

In ten of the states it is elective so far as the private employer is concerned, but compulsory for public employers, such as towns, cities, counties and states.

In eight of the states and one territory the law is compulsory as to both private and public employers. The Federal law, it should be stated, is also a compulsory law.

In twenty-five of the states and two of the territories the employer who has chosen to pay compensation, or who may be compelled to do so under the law, must make due provision for the payment to his employes; or if he chooses to insure them himself, he must prove to the duly constituted commission that he has the financial ability to do it.

Insurance or some other form of security is optional in seven of the states and one of the territories.

A "state fund," as it has come to be called, which is a fund administered by the state but without any state guarantee back of it, is a compulsory form of compensation in force in four states and one territory.

In seven of the states there is a state fund but it is not a monopoly, that is, private companies are permitted to do business also, and they compete with the state fund.

In two states where there are state funds, the privi-

lege is granted to employers to assume their own risk. The regulations are very stringent, but if the employer can comply with the regulations and obtain the privilege, he may then secure his insurance in private companies.

Insurance is compulsory either in private or in semi-state mutual associations in two states, and in sixteen states and two territories this form of insurance is written only by companies duly licensed therefor.

The act would probably have been made compulsory in most of the states were it not for some doubt as to the constitutionality of such action.

10. *Main features of law.*—The essential features of workmen's compensation, omitting various special provisions which are largely for the purpose of giving legal effect to the act, may be briefly set forth, using the New York act for reference, as follows:

(a) The employments covered are both public and private, the principal business of which is of a hazardous nature conducted for pecuniary gain. Farm labor and domestic servants are not included in the group, but may be voluntarily brought under the scope of the act. It applies where five or more persons are regularly employed in these hazardous trades.

It covers accidental personal injuries arising from and in the course of employment, and such diseases or infections as may result therefrom. It would not cover those cases where the injury was deliberately inflicted, or where it was due to or arose out of intoxication.

The real contentions which have arisen in connection with the administration of the act have come from a difference of opinion as to whether the injury was "due to or arose out of or in the course of employment." It is evident that there is room for difference of opinion in the interpretation of this phrase. For instance, if the factory is closed for the day and the workmen, while standing in line waiting to receive their pay, begin to fool and one is injured; does this constitute an injury arising in the course of employment?

A written notice of all injuries must be sent to the employer and the Commission within ten days of the injury or thirty days after death.

11. *Compensation allowed.*—The compensation does not apply for the first fourteen days of injury.

Medical aid is provided; this includes surgical apparatus.

If the disability be total the compensation is two-thirds of the average weekly wages with a maximum of $15 a week, and a minimum of $5, not to exceed in the aggregate of $3,500. There are certain injuries which are constituted permanent total disability.

If the disability be partial, as the loss of a hand, arm, foot, leg or eye, the maximum compensation is $20 per week and the minimum $5. In other cases of partial disability, two-thirds of the loss or reduced earning capacity of the injured person, with a maximum of $15 per week and a minimum of $5.

The total sum cannot exceed in the case of temporary disability $3,500.

If the employe be killed, a reasonable amount, usually $100, is allowed for funeral expenses, and 30 per cent of the wages to the wife or dependent husband during widowhood or dependency. Should the widow remarry, two years' benefits are allowed. In addition to this there is 10 per cent addition for each child under 18 years of age. Should there be no widow or dependent child, 15 per cent is allowed to each dependent grandchild, brothers and sisters under 18 years of age; while to parents and grandparents 25 per cent is allowed.

The total may not exceed two-thirds of the wages up to $100 per month, and any excess over that sum is not used in computing the benefits.

The companies reporting to New York State for the year 1915 showed receipts of $31,850,000 for workmen's compensation. This would not include all the business of the country because some companies do not operate in New York State, and in some states private companies are not allowed to operate. It would be fairly safe, therefore, to increase this $31,000,000 by at least $10,000,000 to secure an adequate idea as to the sums now being paid for workmen's compensation.

The first report covering injuries reported and other data for the first seven months of operation (July 1st, 1914, to January 31, 1915), are as follows:

Number of notices of injury filed by employers	130,723
Number of claims received from employes	22,221
Number of claims in which initial awards were allowed	15,218
Number of claims in which subsequent awards were allowed	3,712
Total number of awards allowed	18,930
Number of claims disallowed	982
Number of claims pending	2,707
Number of completed claims set for hearing	3,314

12. *Prevention methods.*—Traveling hand in hand with the compensation which takes care of the injured party we have a movement fostered by the companies and the states that so far as possible improvements shall be made to properties, safety devices installed, and a spirit of cooperation introduced, in order that accidents may be prevented. This is deemed, and justly so, the far better course to pursue than to allow an individual to be injured and then compensate him or his dependents.

In connection with prevention, it should be pointed out that so far as the machinery is concerned there are certain limitations to this kind of work. A large number of the accidents (the greatest percentage) arise not from defective machinery, but from other cases. Hence, if we had perfect machinery and could assume that all these might be eliminated, it still would leave a great majority of injuries to be taken care of that arise from other causes.

The Industrial Board of Illinois in a compilation of 16,774 non-fatal accidents for the year 1915 showed the causes as follows:

Machinery	16.0 per cent
Falls	18.5 per cent
Falling objects	22.4 per cent
Lifting or handling materials	10.9 per cent
Hand tools (hammers, knives, etc.)	5.6 per cent
Stepping on nails and other sharp objects	3.0 per cent
Acids, flames, explosives, hot liquids, glowing metal, etc.	7.0 per cent
Flying fragments (emery splinters, etc.)	4.4 per cent
Animals (kicks, bites, etc.)	1.7 per cent
Not stated	10.5 per cent

13. *Workmen's compensation insurance in Canada.* —Eight of the nine provinces have in force in 1918 workmen's compensation acts of various types. In Ontario, Nova Scotia and British Columbia, the State Board administers the act and insurance companies are prohibited from competing with the state. In Manitoba, Quebec, New Brunswick, Alberta and Saskatchewan the companies only transact the business but the individual employer (with the exception of the province of Manitoba) is permitted, if desired, to carry his own risk.

Canadian employers, generally speaking, prefer an opportunity of choosing between workmen's compensation insurance provided by the state or by the companies.

The establishment of a state workmen's compensation system in Ontario in 1914, probably set a new standard in this matter. As other Canadian provinces have studied its form and one or more propose to adopt it with perhaps some modifications, a few notes on this act will prove instructive.

The Workmen's Compensation Act of Ontario was framed by Sir William Meredith, chief justice of Ontario, and embodies what may be described as a new code of law respecting compensation for accidents to workmen.

The part of the act which is to be administered by the State Board is called Part 1. It does not apply to all employments, but it applies to employments in the very large number of industries enumerated in Schedule 1 and Schedule 2, chief among which are manufacturing, building, construction, lumbering, mining, quarrying, transportation, navigation, operation of public utilities, etc.

The distinction between the two schedules is that in Schedule 1 the Board levies an assessment and collects an accident fund out of which the compensation to workmen is paid, the employers in this schedule not being individually liable to pay the compensation; while in Schedule 2, no accident fund is collected from the employers but they are individually liable to pay the compensation as each accident occurs.

The compensation for the injury is payable under the Ontario act irrespective of any question of negligence or absence of negligence, and the old defenses of common employment and voluntary assumption of risk are no longer applicable. The only cases in which compensation is not payable, provided the accident arises out of and in the course of the employment, are:

(1) Where the disability lasts less than seven days;

(2) Where the accident is attributable solely to the

serious and wilful misconduct of the workman and does not result in death or serious disablement.

No agreement to forego the benefits of the act is valid; no part of the amount payable to the accident fund by the employer is to be charged against the workmen; and the compensation cannot be assigned, charged, or attached, except with the approval of the Board.

Compensation is to be paid for the industrial diseases specified in the act as well as for accidents.

The provisions of the act respecting compensation are in lieu of the right of action for damages at law.

An important feature of the compensation under the act is that it is payable periodically rather than in a lump sum, and as a rule, it continues during disability or during life, as the case may be.

Where the impairment of earning capacity does not exceed 10 per cent, the compensation is to be fixed by the Board at a lump sum, unless the Board thinks it is not to the advantage of the workman to do so; and the Board may in other cases fix the compensation at a lump sum if it sees fit, or may in cases of special need make lump-sum advances without entirely commuting the compensation.

All questions, as to right to compensation and the amount of it, are determined by the Board and its officers instead of by the courts.

Prior to the establishment of a state system in Ontario, an exhaustive inquiry was made by a special commission of the Ontario government. At the out-

set of the inquiry, it was contended by those who spoke on behalf of the workingmen: (1) That the law of Ontario was entirely inadequate in the conditions under which industries were carried on, to provide just compensation for the employed who meet with injuries, or suffer from industrial diseases contracted during the course of their employment; and (2) that under a just law the risks arising from these causes should be regarded as risks of the industries and that compensation for them should be paid by the industries.

The Ontario commissioner, in his report, stated that most of the compensation laws and perhaps all of them, except the German, had not been in force long enough to enable a conclusive opinion to be formed as to their merits or demerits. It was finally decided that a compensation law, framed on the main lines of the German law, but with certain modifications, would be better suited to the circumstances and conditions of Ontario than the British compensation law or that of any other country.

The establishment of a state system in Ontario caused perturbation among the insurance companies which had been writing workmen's compensation insurance there and which are now prohibited from doing that business. Many employers dislike the fact that they are compelled to insure thru the State Board, not having the choice of insuring with the companies.

The opponents of the state system take this ground:

By eliminating the state as an administrator of the act, workmen's compensation will be compulsory—that is, if a workman is injured, he will obtain compensation. At the same time, the employer of labor automatically assumes liability for accidents to his workmen, but whether or not he takes insurance is optional with him, just as in the case of fire or life insurance. The state, therefore, would not be burdened with the troubles of administering a workmen's compensation law, the workmen would be entitled to and would receive compensation, and the employer would have freedom of action in the matter of taking insurance, as he should have.

Another serious defect in the proposed Ontario legislation is the lack of limitation of compensation. Without limitation, the act is dangerous.

14. *Health insurance.*—It would appear that between 1840 and 1850, insurance to cover periods of sickness was written, or an attempt made to write it, in the United States. Companies were organized for this purpose, the first being the Massachusetts Health Insurance Company of Boston. Others were organized in Philadelphia and Jersey City. Apparently not until 1897, did the business commence really to become of much moment. In the following year, 1898, the accident companies began to issue policies making provision for indemnity during periods of sickness, and this has been the great factor that has developed the business to its present state, ranking as one of the successful minor branches of casualty in-

surance. It provides indemnity for temporary disability, permanent disability, hospital charges and surgical benefits.

The interesting feature in connection with health insurance is not what it has done, but what it proposes to do. The income—$6,000,000—from this form of insurance at the present time shows that it has not been taken up very largely by the community. But at the present time, owing very largely to the success of workmen's compensation, there is a determined effort being made to place it in much the same class as health insurance, that is, to make it compulsory so far as that may be possible under the constitutions of the several states and the United States.

It must be remembered that workmen's compensation dealing with injuries which can be traced quite directly to the business in which the injured person is engaged, furnish a very good starting point from which to assess the damages. But illness, as typhoid fever or any other disease that may be covered by the scope of the law, might be acquired in a wholly different place than the place of one's employment. Probably much work that may be called of a pioneer nature will have to be done before this form of insurance can be successfully established on anything like a large scale.

The experience of foreign companies is cited as affording just grounds for what ought to be done in this country, but many things are different; social customs, habits, and policies, which make a plan like

this possible in foreign countries, are different here, and much consideration will have to be given to that difference. It does seem reasonable to expect, however, that out of the discussion that is now going on some workable tentative plan will be developed whereby the value of health insurance to the community at large will be demonstrated, and once demonstrated will be adopted.

REVIEW

A household servant falls while climbing a defective staircase. In your state is the employer liable?

What is a state fund in workmen's compensation insurance?

A factory employe attending one machine is directed by the foreman to attend another machine of a different kind. He is injured. Would the policy cover his injury?

X comes to his work sober but with nerves shaky after an all-day Sunday spree. He loses a finger while running his machine. Would it be your policy to make payment of his claim without question?

What important movement attends workmen's compensation insurance?

What expenditures are covered by a health insurance policy?

PART II

REAL ESTATE

REAL ESTATE

CHAPTER I

THE REAL ESTATE BUSINESS AND ITS INTERESTS

1. *Real estate a business, not a profession.*—Real estate sometimes is inaccurately spoken of as a profession, but it is essentially a business. A profession applies science, art or learning to the use of others, the profit to the professor or person applying it being incidental. On the other hand, business is engaged in primarily for profit, and the profit goes to those who engage in it.

A profession implies attainment in special knowledge. A person may engage in business with or without special knowledge and no one else is concerned with the question whether he has any knowledge of the business, because no one else is affected by the result. If he is successful, the rewards are his; if he fails, he bears the loss. But let him attempt to practise a profession and others are directly affected, if he is unskilful. The fact that his reward is diminished by his lack of skill is merely incidental to the fact that others suffer.

2. *Ethics of the business.*—Whether real estate is a

business or a profession has no connection at all with the ethics governing it.

Every business can be conducted on a plane as high ethically as the ideals of any profession, and the men who have been conspicuously successful in the real estate business have attained success because they have applied there the highest ideals of commercial fair dealing. This does not mean that there is any ethical requirement for the seller or the purchaser to give away anything which belongs to him, or for either one to disclose to the other his necessity for selling or his requirements for buying. It is absolutely necessary tho, that when the bargain has been made, it be lived up to by both parties according to its true intent. If there be any doubt of the intent of the bargain as it is expressed in writing, the spirit of the transaction should be carried out rather than the catch words of a written instrument. Men frequently perform the thing which they have promised to do, altho it may be to their own detriment and altho they may not be legally obligated. Again, the bigger and more successful the man who makes the promise, the more surely will it be carried out. Important obligations are often incurred upon the mere promise of a well-known man to sell an important piece of property at a definite price, altho no legal and enforcible obligation exists. The promise is always redeemed if it is made by a man who knows the business, and it is redeemed not merely from altruistic motives, but also for purely business reasons.

3. *Divisions of the business.*—The principal divisions of the real estate business are investment, operation and agency. These differ from one another according to the aims of the persons engaged in them and the methods by which those persons expect to make their gains. To conduct either of the first two divisions of the business, investment or operation, actual money capital is required. The most important capital in the agency business is the good-will of its customers, and that can be husbanded, increased and made very valuable.

4. *Investment in real estate.*—Investment is the employment of capital in acquiring some interest in real estate for permanent ownership, or for the actual use of the investor. The investment may take one of the following forms:

(a) Purchase of land or leasehold for use and occupation of the investor.

(b) Purchase of land or leasehold for the purpose of renting to others.

(c) Purchase of land or leasehold to hold for resale in expectation of an increase in value.

(d) Making loans secured by real estate mortgages, either freehold or leasehold.

5. *Operation of real estate.*—Real estate operations means the use of capital in conducting commercial enterprises, using real estate as the stock in trade. It includes:

(a) The purchase of land and its resale.

(b) Erecting buildings.

(c) Making mortgage loans.

The purchase and sale of land deals with land as a thing to be bought and sold at a profit or a loss. It may be divided into two parts:

(1) Speculation, by which the operator buys land hoping its value will rise. He sells, when his hope is realized, or when he finds it to be unfounded.

(2) Development, which has to do with the purchase of tracts of land, usually in their wild state, subdividing them, adding necessary street improvements, such as water, gas and sewers, and retailing them in small parcels to investors and builders. This is an important and useful branch of the business and it has resulted in the opening up and settlement of many sections of the country.

That part of real estate operation which concerns itself with building may be divided into three parts:

(1) Speculative building, which consists in erecting buildings for the purpose of sale at a profit.

(2) Investment building, which includes the erection of buildings for ownership by the builder, either for his own use or to secure a rental income. This form of operation might properly come under the *investment* division of the real estate business altho the investor is temporarily conducting a real estate *operation.*

That form of operation which is concerned with making mortgage loans is divided into two parts:

(1) Making building or temporary loans.

(2) Making permanent loans.

Building or temporary loans are made for the purpose of erecting, altering or repairing structures on the land, or to finance the development of new tracts. They are secured by mortgages on the property to be improved, with the agreement that the money shall be advanced as the work progresses. The lender must supervise the work and runs the risk of having to take over uncompleted structures. Consequently a greater rate of interest is charged on such loans than on ordinary mortgages. On the completion of the work it is to the borrower's interest to replace the loan at a lower rate of interest. Many loans of this character are now made in the form of building and permanent mortgages, the agreement being that the mortgage shall run for a definite time thereafter.

Permanent loans are when money is advanced or lent at current interest rates, upon real estate mortgages or mortgages of leaseholds, the property being considered ample security for the loan. These loans are usually made for a definite time at a fixed rate of interest which is payable periodically.

It should be understood that the class of mortgage loans coming under this division are those made to secure mortgages for resale to investors.

6. *Real estate agency.*—Agency is dealing in or with real estate on behalf of others. It is of especial importance in that it engages the attention of the greatest number of persons concerned with the real estate business. It is divided into two parts, brokerage and management.

Brokerage consists of bringing about transactions between principals for a compensation, usually called "commission." The transactions may be sales, leases, exchanges, rentals or loans. Some brokers give their whole time to sales, leases and exchanges, some to renting property, and others, known as loan brokers, specialize in the securing of mortgage loans. These men are specialists in their respective lines. There are many men who conduct a general real estate brokerage business, however, and engage in every phase of it as opportunity presents.

Management is the division of real estate agency which concerns itself with the derivation of income from real estate as the agent of the owner. It includes the securing of tenants, collection of rents and physical care of the property. The owner is relieved of all the care of managing the property. The agent receives a compensation for his services, usually a certain percentage of the gross rents collected. His duty is to obtain the highest amount of rent and to keep the expenses down, while at the same time seeing that the property is not allowed to deteriorate.

There are a number of offices which earn a steady and substantial income from the management of real estate. The routine work is carried on by trained employes while the head of the office exercises general supervision, and has most of his time free for work on brokerage matters.

7. *Property, real property and real estate defined.* —Property is the right to possess and use a thing.

Real property is a technical legal term meaning the right to possess and use land for a term measured by a life or lives, or for a longer period. In the eyes of the law, all other property is personal property. The right to possess and use a piece of land for the term of one's natural life is real property, because the lifetime is the measure of the term of ownership. A lease of the same land for ninety-nine years, or even a longer period, is termed leasehold and is personal property. If we bear in mind the definition of the technical legal term "real property" it will be easy to remember that all other property, whether connected with real estate or not, is personal property.

Real estate is now spoken of as a business, and by those who engage in it, is looked upon as a vocation. Real estate is also a commodity, and includes real property, and those interests in land which are not real property such as mortgages, leases, liens, etc.

Every business has in view commercial transactions resulting in the transfer of ownership of property of some kind. In our study of real estate, we shall consider interests in land, liens upon it, the making of contracts, transfers of title, conveyances used, and the rights, duties and privileges of the various parties to the transactions. We shall find that the methods of dealing in real estate, and the laws governing it are not arbitrary, nor mysterious or hard to understand. The practical business man should be familiar with the methods and laws for the conduct of the real estate

business, in order to give intelligent consideration to the affairs which engage his attention.

8. *Estates and chattel interests defined.*—One, or several, or a large number of interests may exist in a parcel of land, at the same time. That is to say, many persons may have various kinds of interests in it. Some of these interests are known as "estates" and others as "chattel interests." Estates are interests in land which amount to real property. They may be interests the duration of which are measured by a life, or lives, or they may be perpetual. Chattel interests are all those interests in land which are of less importance in the eyes of the law and whose duration is less than that of estates. If the interest or right comes within the definition of real property, it is an estate; if it does not, it is a chattel interest, and is considered personal property.

9. *Estates in fee simple.*—The everyday ownership of land is known as an estate in fee simple, or fee simple absolute. This is the highest form of property right in land known to our law. It is the right of a person, his heirs and assigns, to own land without limit as to time. This right is subject, however, to the limitations which the law imposes upon the ownership of all land and to which we shall refer later. This is the estate usually dealt in commercially, and a contract to sell land is implied to be an engagement to sell the property in fee simple unless it is otherwise stipulated.

All interests in land less than a fee simple imply

that somewhere else, in some other person or persons, there is, or will be, the residue, which must be added to the particular estate, to make the fee simple absolute.

10. *Fee upon condition and fee determinable.*— Grants of land are sometimes made in such a way that the estate granted terminates upon the occurrence of a contingency. There are two such estates, a fee upon condition subsequent, and a fee determinable. An example of the first is where A gives the land to B, his heirs and assigns forever, only upon condition that no liquor shall be sold at any time upon the property. If the condition is broken, it is the right of A, or his heirs, to recover the property. The right which A retains in the property is known as the possibility of reverter. A, or his heirs, can release this right at any time to the owner of the conditional estate, but they cannot sell it to any other person.

If A gives the property to B to hold forever, but with the provision that if B dies leaving no children the land shall go to C, then B has an estate in fee determinable. The right would terminate if the contingency happened for which A provided, and it would be determined within a time measured by a life, or lives, whether the contingency did or did not occur.

The difference between a fee determinable and a fee upon condition is that, in the case of the fee upon condition, a time may never come when it can be determined whether or not the condition has been broken whereas, in the case of the fee determinable, it can be

found out within a time which may be determined, whether or not the condition upon which the estate shall end has materialized.

11. *Life estates and remainders.*—Estates may be granted so that the present interest is not a fee, but is measured by the duration of a life, or lives, so that another person or other persons shall have the right to take the property after the present interest ends. A right to own land during a life, or lives, is called a life estate. The future interest, which will vest in possession after the end of a life estate, is known as a remainder. Life estates may be measured by the life of the life tenant or by the term of life of another person or of other persons. Remainders may be contingent or vested. A vested remainder is the indefeasible right to take real property after the termination of a particular estate, or the right to take the property if the particular estate terminates immediately. A contingent remainder is one which may vest in possession, if events happen which defeat the vested remainder.

Examples of these two interests are as follows:

If A grants a piece of land to B to hold during his life, but provides that after his death it shall go to C, C's right to possess the property after the life estate is known as a vested remainder, since it is an estate that will vest certainly, sooner or later. B has the land during his life, and he may sell this life interest, but when he dies, C's right accrues, and it is always definitely known who will take the remainder.

If A grants a piece of land to B for the term of the

latter's natural life, with the provision that upon B's death it shall go to C, if living, but if C be not living that it shall go to D, then D's interest is a contingent remainder. D will get the property if C dies before B, but it cannot be known beforehand whether D will get it or not. It will be seen that in this case C's interest in the land is a vested remainder, subject to being divested if he dies before B.

12. *Dower.*—In many states, including the State of New York, a wife has a right in her husband's real property, known as dower. Dower is the right of the wife upon the death of her husband to have for life the use of, or income from, one-third of all real property that the husband owned at any time during their married life. Because the right becomes effective only after the husband's death it is known as an inchoate right. No act of the husband's can defeat the right, but if the wife voluntarily joins with her husband in a deeding of the land to a third party, her dower right in the property, conveyed by the deed, is barred. If they jointly effect a mortgage, the mortgage is superior to the dower right. The law does not permit the woman to release dower to the man at any time during married life, but it may be released to him by an ante-nuptial agreement.

In some states, dower attaches only to such property as the husband may own at the time of his death.

13. *Estates by courtesy.*—There is a similar right which husbands have in the real property owned by their wives, known as an estate by courtesy. If

real property is owned by a wife at the time of her death and not disposed of by will, and she has had a child or children (whether the issue survives or not) the husband is entitled to the use for life of the real property thus left, or to the rents of the property during his life. That interest of the husband can be defeated at any time by the wife's conveying it during her lifetime, or disposing of it by her will. In several of the states, however, of which Vermont and New Hampshire are examples, the common law rule that a wife cannot bar her husband's courtesy by deed, encumbrance or will, is still in force.

14. *Joint tenants and tenants in common.*—Land is frequently owned in fee simple by two or more persons. Sometimes the owners hold it as joint tenants. The principal feature of this form of ownership is that if one of the joint tenants dies, his share does not pass to his heirs or devisees, but vests in the survivor or survivors of the joint tenancy.

If the land is owned by two or more persons as tenants in common, each one is said to own an undivided interest. At death this interest passes to the heirs or devisees, just as it would if the deceased owned the entire fee.

When land is owned by husband and wife jointly, the ownership is known as a tenancy by the entirety. Neither one, acting individually, can alienate the property. At the death of one the survivor gets all the property.

Both joint tenants and tenants in common can sell

or mortgage their respective interests in the land during their lifetime. A grantee of a joint tenant would become a tenant in common with his cotenants.

15. *Chattel interests.*—The principal chattel interests are leaseholds and liens. A leasehold is the right to occupy the property of another in consideration of the payment of rent. It is a chattel interest whether the term is for 999 years, or only for one month. A lien is a claim upon the property of another, arising from a debt or obligation which entitles the holder of the lien, if it is not satisfied, to sell or require the sale of the property. Both leaseholds and liens are more fully considered under separate chapters.

16. *Limitations upon ownership of land.*—In a civilized community, there is no such thing as the ownership of either real or personal property, unlimited as to duration and free from limitations as to use. Our civilization holds individual rights and ownership in the highest respect but, at the same time, it imposes thru its laws such limitations upon the ownership of property as it deems necessary for the good of the community.

The absolute dominion of land is affected by four important limitations imposed and enforced by the state: (1) police power; (2) original and ultimate ownership of the state; (3) eminent domain; (4) power of taxation.

17. *Police power of the state.*—The community has the right to keep property from being used in such a manner as will endanger the life, health or morals of

the community members. The owner of land cannot maintain on it a tenement house or any other building that is insanitary or that is in any other way dangerous to the occupants. He cannot erect a tenement house unless it conforms to certain standards of light and ventilation. The right to erect and maintain buildings is limited strictly by laws designed to guard the public safety and health. This right of regulation comes within what is known as the police power of the state.

18. *Original and ultimate ownership of the state.*—The title to all land can be traced back to some form of grant from a sovereign power—the people of the state or their predecessors, the colonies or the king. The state is therefore said to be the original owner of the land. The land may be assumed to belong to the owner, his heirs and assigns forever; yet if the owner dies leaving no heirs capable of inheriting, the land escheats to the state or sovereign power. From these conditions the principle develops that the state is not only the original, but also the ultimate owner of the land.

19. *Right of eminent domain.*—The right of eminent domain is the right possessed by the state to appropriate land for public use whenever necessity arises. No matter how much an owner may want to keep his land, if it is needed for public use the state has the right to take it. This power is called the right of expropriation. There is the constitutional limitation, however, that this right shall be exercised only

upon the condition that a just compensation be made to the owner for the property taken.

20. *Power of taxation.*—The state has the right to levy taxes to raise money for its support. It is right that those who enjoy the benefits of the government should bear its expenses. Real property, being permanent and within easy reach of the tax gatherer, is frequently the basis of state and local taxation. Taxes levied upon real property are enforced against it, and the state's power of taxation is therefore a very real limitation upon the ownership of the land.

REVIEW

A, who is married, sells various parcels of real estate without his wife's knowledge and without her joining in the deeds. The purchasers did not know he was married. A dies. What are the rights of his wife, if any?

A traction company wishes to obtain land for its right of way. The owner refuses to sell. How may the traction company obtain the right of way?

A obtains a judgment against B. B and his wife own a parcel of land as tenants by the entirety. Before A can issue an execution against the land, B dies. Can A still levy on the property?

If A has a lease for 99 years on a piece of property and dies, leaving one son and a will, which devises all his real estate to a charity, who will be entitled to the possession of the leased property?

An ordinance requires that foundations of buildings shall be sunk to a certain depth. X attempts to erect a building without foundations of the required depth. May the city enforce its ordinance?

CHAPTER II

LIENS

1. *Liens, general and specific.*—A lien as already noted is a chattel interest in real estate, and is personal property. It involves the relation of debtor and creditor, and if the debt is not paid, the creditor can sell or require the sale of the property affected by the lien. There can be no lien unless the debt is one that is enforceable by law. A pledge of property to secure a promise given without consideration does not create an enforceable lien.

Liens are general and specific. A general lien affects all property belonging to the debtor. A specific lien affects only the particular property subject to it either by some act of the debtor, or by the operation of law. A judgment is an example of a general lien. When recovered and docketed, or in some jurisdictions if an execution to enforce it is placed in the hands of the sheriff, it attaches to all property owned by the debtor. The most important example of a specific lien is a mortgage. Because of its wide use in the business world, and of its consequent importance, the mortgage will be considered under a separate chapter.

2. *Lien of judgment.*—A judgment is the determination of the rights of parties thru an action at law.

The only judgments which become liens on real property are "money judgments" or those which determine the right of a creditor to receive payment of a debt. Such judgments, and some other liens, affect all property, personal as well as real, but the present consideration of liens is concerned only with their relations to real property.

A judgment in an action may, for example, enjoin a person from erecting a contemplated building in violation of a restriction. Such a judgment creates no lien on the property since it does not call for the payment of money. If the same judgment, however, awards a sum of money to cover the costs of the action, that part of the judgment becomes a lien.

3. *How lien of judgment is enforced.*—A money judgment is enforced by docketing and execution. By docketing is meant the entry of a note of the judgment in a book of public record known as a "judgment docket" or book. This book is kept in the office of the county clerk, and is indexed alphabetically according to the names of the debtors. Execution is a writ to the sheriff directing him to sell all property in his bailiwick belonging to the debtor at the time of docketing the judgment, or afterward coming into the ownership of the debtor. No more property is sold than to satisfy the judgment, but until the judgment is paid it may be enforced by execution whenever any property of the debtor can be found. Execution may be issued to one or more sheriffs in the state or province.

The sheriff sells all the right, title and interest of the debtor in the property offered for sale under execution. Since the judgment attaches to what the debtor owns and nothing more, the sale does not purport to include the entire title to the property, but only the debtor's interest in it. If prior to the docketing of the judgment, and in some cases prior to an execution being placed in the proper sheriff's hands, the debtor has conveyed the property, the judgment would not affect the title which he had transferred and no attempted sale by the sheriff would be of interest in the property. This would be the case if the deed had not been recorded, even tho it had been actually delivered to a purchaser in good faith, and for value.

The same principle applies to a mortgage which has been delivered but not recorded. The mortgage would be a lien superior to the judgment. Sometimes a question of fact must be determined, whether or not the instrument in question was actually delivered, but unless there is a statute to the contrary, the principle holds true that the lien does not affect the title conveyed by an instrument delivered, but not recorded, prior to the recording of the judgment; the reason being that only the true or actual interest of the debtor can be sold by the sheriff.

The lien of judgment binds all property of the debtor for a definite time fixed by statute. In New York this time is ten years. An unsatisfied lien continues to attach to the debtor's property after it passes out of his ownership. Hence, when title to property is

examined, the public records are searched for judgments against all those appearing in the chain of title. Such a search relates to the names of the owners, not to the property itself.

A sheriff's sale under execution of a judgment is not usually absolute until a definite period afterward. During the interim an owner, or the holder of a junior lien, can redeem the property by payment of the amount for which it was sold, plus interest and costs.

4. *How lien of judgment is discharged.*—Many judgments are obtained which are reversed by appeal to a higher court. For that reason and to lift the judgment from the property it affects as a lien, the law provides in many jurisdictions for the filing of a bond sufficient in amount to secure the judgment. Upon filing such a bond the judgment is marked on the records, "suspended on appeal," or "proceedings stayed." Recourse is thereafter against the bond and the property is free from the lien.

When a judgment is actually paid an instrument known as a "satisfaction of judgment" or "satisfaction piece" is obtained and filed, and the judgment is marked paid on the records. Sometimes a "release of judgment" is obtained where one or more parcels of property are released from the lien of the judgment by the holder of it.

5. *Mechanic's lien.*—A mechanic's lien is a lien upon real property given by statute to mechanics or material men for the price or value of labor or ma-

terial furnished in the improvement of real property. It is usually founded upon a contract made directly with the owner or a person with whom the owner has contracted for the improvement of his property, or any buildings thereon. It is a specific lien which affects only the property for which the labor or material has been supplied.

A mechanic's lien is asserted by filing a notice or claim of lien in the office of the clerk of the county or in some places, in the office of the registrar of deeds, in which the property is situated. This notice must be made under oath, must be filed within a certain time after the labor has been performed or material furnished, must describe the property upon which the lien is claimed, and must state specific details of the claim. If the notice is made out or filed incorrectly the lien may expire or be set aside by the court. The lien attaches when the work is commenced or materials are furnished, but will be lost unless the statutory requirements are followed to keep it alive.

6. *Enforcement of mechanic's lien.*—A mechanic's lien is enforced by an action at law as provided by the statutes relating thereto. All holders of mechanic's liens are brought into the action and their rights are adjusted. The lienholder filing the first lien usually has the conduct of the lien proceedings. If they succeed in establishing their claims the owner must pay the amount due to each, and upon his failure to do so the property is sold to raise the amount due. The court directs the sale and the distribution of any

amount paid by the owner or raised thru the sale of the property. The owner can be held for any deficiency in case the sale does not produce the required amount.

Building contracts usually provide for stated amounts to be paid to the mechanics and material men at certain times during construction, or for the payment of a percentage of the value of the work completed. If a general contractor fails to pay sub-contractors or material men the owner can usually be held only for the amount actually due the general contractor under the terms of the contract with him. If the owner *anticipates* payments to his general contractor, he can be held by sub-contractors or material men as tho such payment had not been made. Some statutes provide that the owner must retain a certain percentage of the amount of the contract for the satisfaction of liens.

The filing of mechanic's liens against real estate is usually an indication that the owner or contractor is unable to meet his obligations, and frequently leads to a discontinuance of the work on an improvement in process of construction. By a recent amendment [1] to the Mechanic's Lien Law in New York State, provision is made whereby with the approval of the lienors, holding 75 per cent of the amount due, a trust mortgage can be made for the benefit of the creditors and additional money can be borrowed on a building-loan mortgage for the purpose of completing the im-

[1] Chapter 507, laws of 1916.

provement. All liens become subordinate to the mortgage securing moneys borrowed with such consent, and have no priority over each other. The law further provides a means for the sale of such property free from all mechanic's liens and judgments upon deposit with the County Clerk of an amount approved by the lienors holding the same percentage of the liens.

7. *How a mechanic's lien is discharged.*—A mechanic's lien may be discharged in any one of the following ways:

(a) By expiration. The lien attaches to the property only for a definite time fixed by statute (in New York, one year from filing). It then expires, but under certain circumstances it may be renewed by order of the court upon the application of the lienor.

(b) By deposit of money. A sum sufficient to cover the lien may be deposited with the county clerk, and the lien will then be marked "discharged by payment." This is often done when the owner of the property disputes the claim of the lienor, and wishes to free his property from the lien during the litigation. This money is held as security; if the lienor does not take an action within the time allowed by statute, it is returned to the owner.

(c) By filing a bond. A bond approved by the court may be filed to cover the lien with costs and expenses. Recourse is then had to the bond and not the property, if the lienor succeeds in establishing his claim.

(d) By order of the court. An owner may wish to have the issue with the lienor tried out in court without delay. In order to do this he can serve the lienor with an order directing him to enforce the lien within thirty days. If the action is not then brought by the lienor, the owner can apply to the court for an order to have the lien discharged. If security is given, or money is paid into court, the lienor then proceeds to prove his claims on the fund.

(e) By payment. When actually paid, the owner is entitled to receive a satisfaction of mechanic's lien in proper form for filing with the county clerk or registrar of deeds.

8. *Conditional bill of sale.*—The conditional bill of sale, strictly speaking, applies to personal property and not to real property. When material to be used in the improvement of real estate is sold to a contractor or owner, the property is often transferred with the express agreement that title to such material shall remain in the name of the vendor until the purchase price is paid. The instrument expressing the agreement is known as a conditional bill of sale. A copy is filed in a place of public record, and becomes a notice to everyone of the condition attaching to the sale. The material remains personal property until it is attached to the building in such a way that it must be considered real estate. If it is not paid for, it may be removed by the vendor, unless his removing it would damage the structure. Articles which are frequently the subject of a conditional bill

of sale are plumbing, heating and lighting fixtures, ranges, boilers, elevators and machinery.

The conditional bill of sale must be filed in accordance with the statute, in order to hold good against innocent purchasers or mortgages for value. It is valid for one year from filing, but usually it can be renewed from year to year.

9. *Lien of decedent's debts.*—The decedent's debts must be paid immediately upon the death of the owner of property. Creditors have a claim upon his property, both real and personal, before his heirs or next-of-kin receive anything from the estate.

Ordinarily, personal property which has not been specifically bequeathed must be applied first to the payment of debts. If such property is sufficient, the personal property which has been specifically bequeathed shall then be applied to the payment of debts. If all the personal property is insufficient, the creditors have a right to require the executors to resort to the real property of the decedent for the payment of debts.

During a specified statutory period, from the time letters of administration or letters testamentary are issued, or, if no letters are issued, during some specified period from the death of the decedent, a general lien applies to all property which has come from the decedent to any person. A creditor may, at any time within the statutory period, require that the executors or the administrators shall sell all or enough of the property to pay all debts of the decedent. The pro-

ceeding is regulated by law, and the property is usually sold under the supervision of the surrogate's court.

10. *Transfer tax.*—Another lien which arises by reason of death is the state's lien for a special transfer tax or succession duty. The State of New York and a very large number of other states in the Union, tax the act of transferring property from a decedent to those who claim to succeed. The tax is really not upon the property but upon the privilege of *succeeding* to the property; to that extent it is more in the nature of an excise than a tax. In its effect, however, it is a true tax, because it is taken out of the thing as it is transferred before it reaches the recipient.

The state can require that all property of the decedent, or enough to pay the tax, shall be sold. The property, no matter in whose hands it may be, is affected by the lien of the tax. This is a general lien because it may affect any piece of property for the whole amount of the tax.

The rate of taxation differs in various states. Usually property going to descendants, husband, wife, father, mother, brothers and sisters is wholly or partly exempt, or taxable at a lower rate than property going to remoter collateral or to strangers.

11. *Franchise tax of corporation.*—In the State of New York most corporations are subject to an annual franchise tax. The law governing this tax was amended June 4, 1917. Under the amended law a report must be filed annually by each corporation doing business in the state according to the form pre-

scribed for the Federal income tax on corporations. If the business of the corporation is not conducted wholly within the state further reports are required in order to establish the proportion of business within the State of New York. The tax is three per cent on the net income, or on the computed proportion of the net income which arises from business operations in New York State. The tax when fixed becomes a lien on all property of the corporation within the state.

REVIEW

A has a life interest in a farm. B obtains a judgment against him. The sheriff's deed to C purports to convey an estate in fee. Is the title good?

Jones builds a house for Smith. Jones becomes financially embarrassed and Smith pays him, on October 1, $2,500 that was not due until October 15. Jones neglects to pay one of the subcontractors, who files a mechanic's lien. What is Smith's position?

X dies, owing a bill to Y. The personal property of X is bequeathed to his wife. The real estate descends to his son. No provision is made for the payment of Y's bill. The personal property is not enough to meet Y's bill. X's son offers to sell you the real estate within a few months after he comes into possession. What would be your answer?

CHAPTER III

TAXES AND ASSESSMENTS

1. *Lien of taxes on property.*—The ownership of real property is subject to the state's power of taxation. Taxes are a regular and enforced proportional contribution to the support of government. The tax is levied directly upon the property and when levied becomes an enforceable lien.

2. *Various state and county levies.*—Taxation may consist of a single annual levy for all purposes, such as is made in the City of New York, or it may consist of several levies, a method which obtains in the districts outside incorporated cities. The several levies may be some or all of the following:

(a) State tax. This is a contribution to the expenses of the state government which is apportioned among the counties each year.

(b) County tax. The several counties may raise by taxation a sum necessary to keep up the functions belonging to the county government, such as maintenance of roads and bridges, support of hospitals and institutions of correction, and care of the poor.

(c) Town tax. Subdivisions of the counties have distinct objects for which funds are raised by taxation. Very frequently state, county and town taxes are levied and collected at the same time.

(d) School tax. This is a separate annual tax levied in school districts outside of cities for the support of the public schools of the district. It is voted by the tax-paying residents of the district.

(e) Village tax. Incorporated villages have a recurrent tax to provide means for purposes peculiar to the village government.

(f) Highway tax. This tax is sometimes levied separately by a highway commissioner to provide for upkeep and repair of roads.

3. *Determination of tax rate.*—There are two factors which determine the tax rate, i.e., the budget and the total assessed value of taxable property. The budget represents the total amount of money to be raised, either estimated in advance, or computed after the appropriations are made. The next step after the budget is compiled consists of assessment and apportionment. The process of assessment consists in ascertaining the total value of property within the jurisdiction subject to the tax. A list of such property is made up by regularly appointed or elected assessors, who indicate the respective values of all property listed, which is frequently subject to revision or repeal. The tax rate is obtained by dividing the amount of the budget, less any revenue obtained from other sources, by the total assessed value of the taxable property. The total amount to be raised is apportioned by applying the tax rate to the value of each separate piece of property.

In some jurisdictions, personal property is taxed at

the same rate as real property, the tax on the estimated amount of personalty being assessed against the owner. There is frequently a business tax.

4. *Assessed valuations.*—The assessed valuation of real property is often made by the assessors at a fraction of its market value, such as one-third, one-half, two-thirds, etc. It is sometimes placed at the figure which it is estimated the property will bring at a forced sale. Such practices frequently lead to inequalities and it is coming to be realized that the only fair basis of assessment is the full and actual market value of the property. Full value has been defined as "the sum for which the property would be appraised in payment of a just debt from a solvent debtor." It has also been defined as "the sum which a purchaser who wishes to buy and is not compelled to buy would give to a person who wishes to sell and is not compelled to sell." As a certain sum of money must be raised, if the assessment is low the rate on the dollar is high, and if the assessment is high the rate can be low.

In many places, for purposes of taxation, the values are separated to show the value of the land and the value of any existing improvement. This method has been found to be the best for the securing of fair and even assessments.

The land is valued on the basis of the value of standard or typical lots in the vicinity; the buildings are valued at the amount they add to the land value. This amount is determined by figuring the cost of construction and making proper deductions for deprecia-

tion and obsolescence. If the building is not a suitable improvement, its value may be far less than cost.

5. *Reduction of assessed valuation.*—The appraisers' list of properties showing the values allotted to each, are usually open to public inspection some time before the tax is fixed. If an owner feels that his property has been overvalued, he is given an opportunity to protest. He may base his objection upon the records of sales made or prices asked for land in the vicinity. He may show from values assigned to similar buildings, from rental statements, or from records of the cost of construction that his building is overvalued. The arguments advanced by the owner may lead to a reduction in his assessment.

The owner may show an inequality in his assessment compared to that of others, or he may show that the assessors have adopted an incorrect unit of value for the land. All similar land in the same neighborhood, as, for instance, inside lots in the same city block, should be assessed uniformly. If the value of one lot is reduced by the assessors, the values of all similar lots in the immediate vicinity should be similarly reduced. The assessors seek to ascertain the correct unit of value and then apply it equitably. The principle of unit value applies to the lot only, as each building in the vicinity may be different from every other building and must be considered separately.

The property owner may appeal to the courts if he is not satisfied with the decision of the assessors regarding his claim of over-assessment. Such an appeal

is frequently by a writ of *certiorari*. This term is applied to a proceeding whereby the court reviews the act of the public official to ascertain whether that official has acted in accordance with the principles of law by which he is bound. The court may order a reduction of the assessment if, upon the evidence submitted, it finds that the property has been over-assessed.

6. *Taxes in New York City.*—In the City of New York, there is a Board of Tax Commissioners consisting of a president, six commissioners and a number of deputies. The city is divided into districts and a deputy assigned to each. The deputy makes up the assessed valuation lists for the real property in his district. The deputies begin to assess on April 1 of each year. On October 1, the records of assessed valuations are open for public inspection, and remain open until November 15. Application for the reduction of the assessed value of real estate must be filed on or before November 15. The books close on November 16, and after that date the applications for reductions are considered and hearings held. On the first of the following February, the final assessment rolls are made up, and on March 1, these are delivered to the Board of Aldermen. On March 3, the Board of Aldermen fix the tax rate and on March 28, they deliver the assessment rolls to the Receiver of Taxes. Using the tax rate and the assessed valuation of each piece of property, the amount of the tax apportioned to each parcel is computed. The tax is payable in two instal-

ments, one due May 1 and one due November 1. If the tax is not paid in the month in which it is due, interest at the rate of seven per cent per annum, computed from the due date of the instalment is added. If the instalment, due November 1, is paid after May 1 and before the date due, a discount at the rate of four per cent per annum is allowed. Each half of the tax becomes a lien by law on the real estate on the day it is due. Outside New York City, it is the usual rule that as between buyer and seller, the tax is a lien as soon as it is fixed definitely, altho it may not be collectible until a future date.

The tax budget for New York City is made up as follows: The various departments submit estimates to the Board of Estimate and Apportionment. After investigations and the holding of public hearings a tentative budget is prepared. This budget is referred to the Board of Aldermen after it has been approved by the Board of Estimate and Apportionment. The Board of Aldermen may reduce or eliminate some of the items, but may not increase any. The reductions and eliminations are subject to the mayor's veto. The budget for the ensuing year must be certified before December 25 and be published in the City Record before December 31 of each year. The amount of the budget, less certain items of city revenue, divided by the total assessed valuation of taxable property, real and personal, gives the tax rate fixed by the Board of Aldermen. The rate varies slightly in the different boroughs by reason of the differences in the

amount to be raised for the county governments in which the respective boroughs are located.

7. *Definition of assessments or local improvement taxes.*—Assessments are special taxes levied upon specific property benefited by local improvements for the purpose of paying or contributing to the cost of such improvement. The apportionment of the assessment is not always equal over its entire area, but is in proportion to the benefit derived from the improvement. Lots fronting on a street would be charged with a greater proportion of the cost of an improvement in that street than would lots farther away. Sometimes the lots fronting on the street are the only ones assessed, and sometimes the area of assessment extends for some distance from the location of the improvement. Allowances are made for corner lots, short lots and lots of irregular shape in order to make the assessment equitable.

Taxes are regular and are to be expected at recurrent intervals. The tax period is usually the current year, January 1 to December 31. Special assessments are laid at irregular intervals, and therefore due notice must be given to the property owner. Laying an assessment amounts to the commandeering of private property, and a test of the validity of an assessment is whether or not adequate notice has been given of the intention to lay it. Assessments may be laid by a proceeding in court, or by a board of assessors.

8. *Assessments laid by authority of the courts.*—

When land is acquired for public uses by condemnation proceedings, the courts appoint commissioners who fix the cost of the property taken, and assess the land within a determined area according to the benefit derived by each parcel from the improvement. These persons are therefore both commissioners of estimate and commissioners of assessment. The report of the commissioners is subject to the approval of the court, and opportunity is given to property owners to file objections to the report if they so desire.

9. *Assessments levied by a board of assessors.*—The principles applicable to assessments levied by authority of a board of assessors are similar to those applicable to assessments levied by authority of a court. However, the board of assessors is often limited by a mechanical rule, by which it cannot lay an assessment upon any specific piece of property for more than a definite proportion of its assessed value. While in one respect this is a protection to the taxpayer, in another it operates to retard needed public improvements, especially in suburban districts where land values are low and in districts not fully developed.

Within the limit allowed them, the assessors are supposed to proceed according to sound economic principles in laying assessments for public improvements. The assessments which most frequently are levied are for making physical improvements on a street, such as sewerage, regulating and grading, paving and laying sidewalks. After such improvements are made, the land value usually increases. The as-

sessed value for taxation the following year should rise not only by the amount of the assessment, but by as much as the usefulness of the lot has been increased, which is very often more than the amount paid for the mere physical work.

The making of the improvement is initiated by the property owners or by their representatives. Due notice is given of the intention to make it, and notice is also given of the assessment levied to pay its cost. If the decision of the assessors is not satisfactory, after a hearing on objections, an appeal can be taken by judicial proceeding.

10. *When an assessment becomes a lien.*—Usually assessments are a fixed lien and chargeable between buyer and seller as soon as the assessment is determined definitely; but in the City of New York an assessment is not a lien until ten days after it is confirmed and entered.

11. *Water rates.*—In their proper analysis, water rates are not a tax at all. Where water is furnished by a municipality, the rates are enforced like taxes, but they are payment for a commodity. In most large cities, there is municipal ownership of water and monopoly of its service, and this is necessary as a health measure. The city charges for the water in accordance with its consumption. It lays the charge in one of two methods, either by fixing an annual charge, or by measuring the consumption thru a meter. The owner of property does not have to use the water in his building if he does not want to. If he has a water

main enter his building, he must pay a certain fixed frontage charge, whether he consumes the water or not, because water may be used for his fire protection.

12. *Enforcement of lien of taxes.*—Taxes, assessments, water rates and charges for installing water meters are all liens, which may be enforced by a sale of the property affected if they are not paid. Sometimes the fee of the property is sold, subject to a right of redemption. The sale sometimes takes the form of a lease of the land for a period of years. In the City of New York, the law provides for a sale of the city's lien of taxes upon the land rather than for the sale of the land itself. At certain periods a list of unpaid taxes, assessments and water rates, plus accrued interest is made up against each lot on the tax maps. The total amount unpaid against the lot is sold as a tax lien to the person bidding *the lowest rate of interest,* which rate cannot be more than 12 per cent. The city executes to the purchaser an instrument known as a transfer of tax lien. This gives the purchaser a first lien on the property (superior to all other existing liens) due in three years with interest at the rate bidden, payable semi-annually. The lien can be foreclosed, in the same manner as a mortgage, upon failure of the owner of the land to pay interest, principal, subsequent taxes, assessments and water rates when due. In the provinces of Canada the taxes are usually allowed to remain in arrears for some considerable time before proceedings are taken for the

sale of the property; proceedings, however, vary in the various provinces.

REVIEW

What is the procedure of levying taxes and fixing the tax rate?

Describe the methods of fixing taxes in New York City.

Explain the difference between a tax and an assessment. How are the latter usually levied?

How is the tax lien enforced when the amount is not paid?

CHAPTER IV

CONTRACTS

1. *Real estate contracts should be in writing.*—Agreements for the transfer of an interest in real property belong to the class of contracts, which in addition to the common characteristics of all contracts —agreements, competent parties, lawful consideration and a promise—must be in writing in order to be enforceable and must be subscribed by the party to be charged or his authorized agent. From a commercial viewpoint, it is wise and safe that the bargain upon which two contracting parties have agreed should be expressed in writing. In the course of time, it has been found wise that a contract relating to such an important commodity as land should stand upon a sound basis, and therefore be in writing and not left to word of mouth. A statute generally known as the Statute of Frauds was passed requiring practically all contracts relating to land to be in writing. This statute is in one form or another in force in most jurisdictions. For the full completion of the real estate transaction there are two important steps: first, the signing of the contract, and second, the closing of the title. The first step is taken when the minds of the parties have met and made the bargain; the sec-

ond after the purchaser has had the opportunity to look into the title to the property involved and to arrange for the cash required to be paid on closing the title. Between the making of the agreement and its consummation at closing title some time may elapse. Because of this and because of possible misunderstandings between buyer and seller, expenses incurred by the purchaser, or changes in the legal position of both parties, it is only ordinary prudence that a written instrument expressing the full details of the bargain be drawn up and signed by both parties.

No special form of real estate contract is prescribed by law. If the instrument has the essential elements of a contract, and expresses the entire bargain, it is sufficient. In order that we may note what is usual in contracts of this sort, a copy of a form of sales contract used by the leading title companies of New York City is given here by way of illustration. It must of course be recognized that in places outside New York City some of its provisions should be excluded, and others, suitable to the particular case, inserted. The printed part includes what has been found usual in all such contracts, and the blank spaces are provided to be filled in with such matter as pertains to the particular case.

AGREEMENT, made and dated
between

hereinafter described as the seller and

hereinbefore described as the purchaser.

Witness, that the seller agrees to sell and convey, and the purchaser agrees to purchase all that lot or parcel of land, with the buildings and improvements thereon

The price is

Dollars, payable as follows:

Dollars on the signing of this contract, the receipt of which is hereby acknowledged

Dollars in cash on the delivery of the deed as hereinafter provided.

The deed shall be delivered upon the receipt of said payment at the office of
at 19
Rents and interest on mortages, ,
if any, are to be apportioned.

This sale covers all right, title and interest of the seller, of, in and to any land lying in the bed of any street, road or avenue, opened or proposed, in front of or adjoining said premises, to the center line thereof, or all right, title and interest of the seller in and to any award made or to be made in lieu thereof, and the seller will execute and deliver to the purchaser on closing of title or thereafter on demand, all proper instruments for the conveyance of such title and the assignment and collection of such award.

If there be a water meter on the premises, the seller shall furnish a reading to a date not more than thirty days prior to the time herein set for closing title and the unfixed meter charge for the intervening time shall be apportioned on the basis of such last reading.

The deed shall be in proper statutory short form for

record, shall contain the usual full covenants and warranty, and shall be duly executed and acknowledged by the seller, at the seller's expense, so as to convey to the purchaser, the fee simple of the said premises, free of all encumbrances except as herein stated.

All personal property appurtenant to or used in the operation of said premises is represented to be owned by the seller and is included in this sale.

All sums paid on account of this contract, and the reasonable expense of the examination of the title to said premises are hereby made liens thereon, but such liens shall not continue after default by the purchaser under this contract.

The risk of loss or damage to said premises by fire until the delivery of the deed, is assumed by the seller.

The stipulations aforesaid are to apply to and bind the heirs, executors, administrators, successors and assigns of the respective parties.

Witness the signatures and seals of the above parties.
In presence of

[L. S.]
[L. S.]
[L. S.]

2. *Divisions of the contract.*—The form given above has four main divisions.

Date and statement of parties.

The agreement and the description of the property.

The financial terms of the bargain.

Miscellaneous stipulations.

3. *Date and statement of parties.*—The contract is dated merely as a convenient memorandum of the time it was made. There is no legal necessity for this to be done. The names of the parties are filled in, one being described as seller, the other as purchaser. They might be described as vendor and vendee, or as

the party of the first part and the party of the second part, but the simpler forms are always desirable when they serve the purpose equally well.

4. *What the purchaser should know about the seller.* —Under this contract the purchaser deposits his money with the seller as a partial payment on the purchase price. His chief concern is to be assured that the seller is the owner of the property, and has a good right to sell it. If the seller has been introduced as the owner of the property by a broker upon whom the purchaser can rely, he takes very little chance in dealing with him. If he wishes to be further assured he can ascertain from the records whether the seller appears as the owner. While it is not an easy matter for a layman to find this out from the public records, he can get from any title company, for a small fee, a card which shows the name of the last owner of record. If the seller is an executor, trustee or guardian, it is proper to inquire whether or not he has power to sell the property. It is possible that while he may not have the power to sell when the contract is signed he may obtain the necessary permission from the courts. If the matter is at all doubtful the purchaser should have the advice of counsel before entering into the contract. It is a familiar rule of law that a person under legal age, i.e., 21, or an insane person cannot make a contract. A corporation owning the property, and acting thru its duly authorized officers, may make a valid contract of sale.

5. *What the seller should know about the purchaser.*

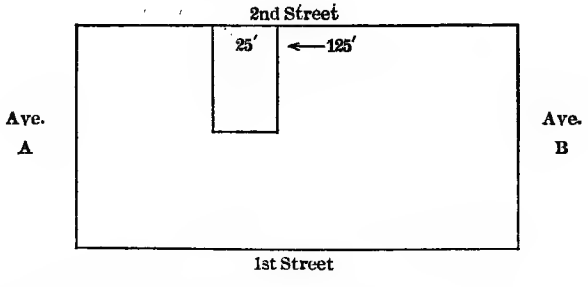
—The personality of the purchaser is rarely of consequence to the seller. He merely wants to get a large enough payment when the contract is signed to assure him that the purchaser will carry it out. This payment, or deposit, is often called the earnest money. The property will be withdrawn from the market when the contract is signed, and if the title is not closed, an opportunity to sell to someone else may be lost. This is especially the case on an active and rising market. When the bargain is made the seller oftentimes becomes liable for a broker's commission. To reimburse the owner for the commission, and to protect him against loss by withdrawing his property from the market, the purchaser should be required to pay a substantial sum when the contract is signed. Purchasers sometimes buy in the name of a dummy. If the broker knows this he should inform the seller, altho he is not obliged to impart the name of a principal especially when he has learned it in confidence. The seller, who deals with a dummy, requires the payment of a larger amount of earnest money than when he deals directly with a person of responsibility. Sometimes a sale of land is made with an agreement that the seller will make a building loan. In this case, the personality and reputation of the purchaser, who will also be the builder, is important to the vendor.

6. *Agreement.*—"The seller agrees to sell and convey, and the purchaser agrees to purchase." This promise, in exchange for a promise, is the consideration which supports the contract. The earnest money

is merely a payment on account of the purchase price. It is not the consideration. The property is *sold* when the contract is signed; the title, however, is to be *conveyed* by a proper instrument at a later date.

7. *Description the most difficult part of the contract.*—The seller has in mind the property he owns and wishes to sell. The purchaser has in mind the property he expects to get. The contract should be drawn so that the seller is obliged to convey just what he owns and no more, and so that the purchaser will get what it was his true intention to buy. No general rule can be laid down. The description taken from the last deed, or from the seller's policy of title insurance, if he has one, is the best to follow. How widely the conditions to be described may vary can be seen by means of a few illustrations.

8. *Vacant lot description.*—What may be involved in describing a vacant lot can be seen most conveniently by considering the diagram which follows:



This shows a vacant lot on Second Street west of Avenue B. A sufficient description would be. "Lot

on the southerly side of Second Street, 125 feet westerly side of Avenue B, being 25 feet in width front and rear by one hundred feet in depth on both sides; the side lines being parallel with Avenue B." The lot may also be described at length. This is customary in the preparation of a deed.

The lot may be shown on a map of a tract of land. If so, it may be described by the lot and block number shown on such maps, as "lot 110, Block 5, Map of lots of D Estate, filed in the office of the Clerk of New York County." If the purchaser desires, the property can be described both by reference to the map and by dimensions. The seller must be sure in this case that the map descriptions are correct or he should add the words "more or less" to the dimensions. Careful purchasers, however, may not want to take a description qualified by the words "more or less" unless it is stipulated that the dimensions are not less than a certain quantity.

9. *Description of improved property.*—When a person buys improved property he expects to get three things: the land, the structures on the land and a good right to maintain such structures permanently. When the building is in the center of the plot, or well away from the side lines as in the case of a detached suburban dwelling, no difficulty of description is presented. The description which fits the lot is all that is necessary. In describing city property, where buildings are contiguous to each other, problems arise from the fact that the lines of the building may not

coincide exactly with those of the lot. The building on the lot to be sold may encroach on a neighboring lot, or the lot itself may be encroached upon by adjoining buildings. Before closing a purchase it is a wise precaution to have a surveyor's sketch to see that the buildings are wholly on the land being conveyed. It is a maxim of the law that, "he who owns the soil owns from the center of the earth to the sky." There are, of course, exceptions to this.

(a) When a building and lot exactly coincide, the lot can be described by a street number as "Being in the Borough of Manhattan, City of New York, known as 105 Second Street." If the purchaser desires, this description may be amplified by a description of the lot by dimensions. Both descriptions mean the same thing, and both can be given, or one or the other can be omitted.

(b) An adjoining building may encroach on the lot to be sold, say, for example, two inches. The seller, it is assumed, owns a house known as 105 Second Street and he owns a lot 25 feet wide, but his neighbor by encroaching, prevents him from using two inches of his property. In this case the property would be described by street number only, and the purchaser would get the house he has in mind. If he desires to be assured of the dimensions of the lot they can be inserted in the contract in one of three ways.

1. Plot on the southerly side of Second Street, 24 ft. 10 inches wide, 125 ft. 2 inches westerly from the westerly side of Avenue B, etc.

2. Plot on the southerly side of Second Street, 25 ft. wide, more or less, about 125 ft. westerly from the westerly side of Avenue B, etc.

3. Plot on the southerly side of Second Street, 25 feet wide, 125 feet westerly from the westerly side of Avenue B, etc., subject, however, to encroachment of two inches on said premises by building adjoining on the east side. The street number and, indeed, any other particulars can, of course, be stated in addition to any of these descriptions.

4. Lot No. —— according to register. Plan No. —— in the City of Toronto.

(c) The building may encroach on an adjoining lot and it may be assumed again that the encroachment is two inches. In this case there is a building 25 feet 2 inches wide on a lot 25 feet wide. The plot 25 feet wide can be described as you would the vacant lot, letting it follow as a matter of inference and of law that you have a right to maintain the building in its present position encroaching on your neighbor. It would not be well to describe it by street number, or by street number and dimensions of plot, unless in so doing you added a qualification that your house encroached on your neighbor's lot, but that you conveyed a good right to maintain it there. There are cases where the owner of a building has not a legal right to maintain his building encroaching on his neighbor's lot, and in such cases he must state that his sale is subject to the encroachment. If he does not do this, when the time comes to deliver the deed

the purchaser may reject the title on the ground that the title is unmarketable.

10. *Property subject to tenancies.*—If there is simply a description of the property and no more, the purchaser could expect to get a title in fee simple without any limitations or incumbrances. However, property, and especially income bearing property, is often not free and clear. Frequently it is occupied by tenants who are paying rent to the owner under some kind of an agreement. The agreement may be a lease for a definite term, or it may be a monthly letting. If it is a lease, the contract of sale should include after the description, "subject to lease at (here insert the rent) expiring (here insert the date the lease ends)." The lease may affect only part of the premises. If this is so, it is desirable to state what part it affects. If part or all of the premises is occupied by monthly tenants, it is sufficient to state "subject to rights of present monthly tenants." The seller should guard against selling subject to any tenancy different from the lettings subject to which he owns the property.

11. *Restrictions on property.*—Many parcels of land are affected by restrictions as to their use. Such restrictions are imposed on land in order to produce a uniform development or to protect other land of the owner. They may be such as affect the size of the plot on which buildings may be erected, the location of the buildings on the plot, or their size, character and use. It is not fair to ask a purchaser to take prop-

erty subject to any restrictions that may exist. What the restrictions are should be specified in the contract, and an opportunity should be given to the purchaser to examine the record of the instruments in which they are contained. When a purchaser is not absolutely certain that the restrictions will not interfere with his contemplated use of the property, or injuriously affect its value, he should get expert advice before signing the contract. In no case should he let himself be persuaded by any opinions of the seller as to their meaning. Should there be restrictions and none were mentioned in the contract of sale, the purchaser could refuse to take the title.

If the seller is imposing the restriction at the time the sale under consideration is made, and the purchaser assents to it, the proper wording is as follows: "The deed conveying title to said premises shall contain restrictive covenants binding upon the purchaser, his heirs and assigns, as follows:" (the restriction is here set forth at length). In cases where the sale is made subject to existing restrictions the wording would be "Subject to restrictions contained in deed recorded in the office of the Register (or Clerk) of —— County, in Liber —— of Conveyances, Page ——."

12. *Easements.*—An easement is a right thru, over, under or to the use of part of property in favor of another adjacent property. If A has the right to cross B's property to get a public highway that right is known as "right of way" and A's property should be sold subject to that easement.

The most frequent form of easement is the party wall right. A party wall is a wall erected on the dividing line of two lots, standing partly on each, and one that is common to two adjoining buildings. It is created by express agreement between the two owners, or where one owner erects the two buildings with a common wall between them. The owner of each building has the right to have the wall remain as long as his building stands. He can use it for its entire length, but he cannot lengthen it. He may build on it as high as he pleases provided he does not burden it so as to impair its usefulness. The party-wall right should be mentioned in the contract. If a wall stands entirely on one lot, but an adjoining owner has the right to insert beams in it to support his building, the right is known as a "beam right."

Rights or easements in favor of the property go with it whether mentioned in the contract and deed or not.

13. *Facts shown by survey.*—When a survey has been made, it will show any encroachments of buildings affecting the land covered by the contract, whether buildings on the lot encroaching on adjoining property, or of other people's buildings encroaching on it, or of the buildings on the lot encroaching on the public street. If the encroachment is not specifically mentioned in wording the description, it is well when such encroachment exists to follow the description by a clause somewhat as follows:—"Subject to state of

facts shown by survey dated —— made by —— Civil Engineer."

14. *Terms of the financial settlement.*—Under the contract the seller agrees to part with certain property, and in exchange the purchaser agrees to pay a definite sum of money in a specified manner. The gross price of the property is first expressed in the contract and the method of payment follows. The payment may be divided into four parts:—

The amount paid on the contract as deposit or earnest money.

The amount of cash to be paid when the deed is delivered.

The amount of mortgage encumbrance subject to which the property is taken.

The purchase-money mortgage to be given back by the purchaser to the seller.

15. *Earnest money.*—In discussing the parties to the contract we noticed that the seller had reason to require the purchaser to make a payment of earnest money when the contract was signed. The purchaser would desire that the payment be as small as possible. He may not know that the seller is of sufficient financial responsibility to insure the return of his payment in case the title to the property proves to be bad or unmarketable. No absolute rule as to the amount of this payment can be laid down. It is rarely more than ten per cent of the purchase price, and frequently five per cent or less. Sometimes when the seller is as-

sured of the purchaser's financial reliability, a nominal amount, or nothing at all, is paid on the contract.

16. *Cash payment on delivery of deed.*—When no mortgages are involved, this amount may be the difference between the gross price and the amount of earnest money paid, or it may be the gross price after deducting earnest money and the third and fourth divisions of the price referred to hereinafter, or either of them. The printed form given on page 218 requires payment in cash, i.e., in legal tender money. While it is customary for the seller to accept payment of this amount in a certified check, the contract should provide for cash as this leaves the acceptance of a certified check optional with the seller. If the words "certified check" were used they would include a check drawn on and certified by any banking institution, even a small one in an obscure town. The seller should reserve the privilege to require cash when the deed is delivered, or to waive it and take payment in another form if he wishes to do so.

17. *Property taken subject to mortgage.*—As we express the gross price in our contract, the amount of the existing mortgage subject to which the property is sold must be stated as a payment of part of the purchase price. The price and the first three divisions may read thus:

The price is Fifty Thousand Dollars, payable as follows:
ONE THOUSAND.....$1,000
DOLLARS on the signing of the contract, receipt of which is hereby acknowledged.

NINETEEN THOUSAND.....$19,000
DOLLARS in cash on delivery of the deed as hereinafter provided.
TWENTY-FIVE THOUSAND.....$25,000
DOLLARS by taking the property subject to a mortage for that amount now a lien thereon

From the seller's point of view the statement of the mortgage as given above is satisfactory. The purchaser, however, may want to know something about the terms of the mortgage. Unless the terms are stated in the contract he would have to take title regardless of what those terms were. It is therefore often necessary to make the clause read:

Twenty-five thousand dollars by taking the property subject to a mortgage for that amount now a lien thereon becoming due (here insert due date) and bearing interest at the rate of.....per cent per annum.

If the mortgage were to become due at an early date the purchaser might not want to take the property and assume the risk of having to replace the mortgage soon after becoming the owner. On the other hand, he might be buying the property for the purpose of conducting a building operation. In that case he would not wish to take the property with a long-term mortgage unless there was a privilege of paying it before maturity. Many purchasers like to have the mortgages on their property held by one of the well-known mortgage companies or savings banks, and if the property has been represented as being mortgaged to such an institution he may require that the name of the

holder of the mortgage be added to the foregoing clause.

The interest of an owner in real property which has been mortgaged is called the equity. In the case described it is really this equity that is being sold. The purchaser under such circumstances does not become liable personally for the payment of the mortgage debt, altho the property he has bought can be held for it unless he has agreed to assume the mortgage. He may lose the property if there is a default in the payment of interest on the mortgage, but he cannot be held personally liable for a deficiency if the property does not sell for enough on foreclosure to pay the claim of the mortgage.

18. *Assuming the mortgage.*—The holder of a mortgage has the right not only to hold the property as security for the payment of the money he has loaned, but also to hold the maker of the bond, given in connection with the mortgage, personally liable for the debt. The seller, who is thus personally liable, may require as part of the bargain for the sale of the property that the purchaser not only take the property subject to the mortgage, but that he assume payment of it. In order to provide for this in the contract, the following is added to the clause describing the mortgage given in the preceding paragraph.

". . . payment of which the purchaser shall assume when the deed is delivered."

When this is carried out the purchaser becomes liable as tho he were the original maker of the bond and

mortgage. In the event of a foreclosure, he may not only lose his equity in the property, but he may be held for the payment of the deficiency if the sale of the property does not produce enough to pay the claim of the mortgages. It should be remembered, however, that the original bondsman is not thus relieved from his personal liability. He too can be held for any deficiency, but he can seek reimbursement from the one who assumed payment of the debt.

19. *Bond and mortgage as part of purchase money.* —When the sum of the cash payments and the mortgage already on the property do not make up the whole purchase price, the remainder is usually represented by a purchase money bond and mortgage. This simply means that the seller is extending credit to the purchaser for part of the price, and that he requires security from the purchaser for its payment. A purchase money mortgage may then be described as a mortgage given by a purchaser to a seller to secure payment of that part of the purchase price of land not paid when the deed is delivered.

In the case assumed the balance due is $5,000. The additional clause describing the purchase money mortgage may be worded as follows:

FIVE THOUSAND DOLLARS. . . . . $5,000.

By the execution and delivery by the purchaser to the seller of his purchase money bond for that amount secured by a purchase money mortgage on said premises to bear interest at the rate of 6% per annum, to run for four years, and to be conditioned for instalments on account of princi-

pal of $500, every six months. Interest to be paid with said instalments of principal.

This clause provides that the purchase money mortgage be paid in instalments. It may, of course, be worded so that it be payable in one sum at a definite time, if such is the bargain.

20. *Provisions regarding purchase-money mortgages.*—In the case which has been assumed for an illustration, the purchase money mortgage would be a second mortgage. That is to say, it would be subject or subordinate in lien to the earlier mortgage of $25,000. In order that it remain a second mortgage, the purchaser may require the following clause:

Said mortgage shall contain a clause that if the first mortgage be discharged this mortgage shall remain subordinate to any new mortgage placed on the premises in lieu thereof, for like amount and having similar terms.

For his protection the seller usually requires that three things be stated in the contract in connection with this mortgage:

That the bond and mortgage be prepared by his attorney, or be drawn on a particular form with which he is familiar, or in a form approved by his attorney.

That the expense of preparing and recording the bond and mortgage be paid by the purchaser.

That the purchaser pay the mortgage tax, if any.

21. *When the deed is to be delivered.*—The exact day, hour and place for closing the title and delivering the deed are stated in the contract. No rule can be laid down, but many closing dates are fixed thirty

days after the contract is signed. If a title company examines the title it is often arranged to close at the company's office.

22. *Apportionments to be made at closing.*—The next clause in the printed form may be completed to read, "Rents, taxes, assessments, or local improvement taxes, interest on mortgages and fire insurance premiums, if any, are to be apportioned to date of closing." On closing title, rents for the current month are divided between the parties as of that date, the seller allowing the purchaser his share of any of the current month's rent that he has already collected. Taxes for the current year are apportioned, the vendor being charged his proportion from previous January 1. The seller also shows the purchaser the accrued interest on the mortgages on the property to the day of closing, and the purchaser repays to the seller the proportionate part of any premiums on fire insurance policies not yet expired.

23. *Title to land in street.*—In some cases the seller owns the fee to the land in the street adjoining the property, and it is often required that he convey whatever right or title he may have to the purchaser. A proceeding to open the street may be pending, and in order that the man whose land may be charged with an assessment for the proceeding may get any award for the land taken, the contract provides that the seller shall assign to the purchaser, at closing, all his right, title and interest in any such award. This provision can be altered to suit any particular case.

24. *Water-meter charges.*—This provision is made so that the owner of the property shall pay for metered water consumed during his ownership. In many cases no water meter is on the premises, a flat charge for the year being made by the city. If so this clause has no application, and no apportionment is made between the parties.

25. *Form of deed stipulated in contract of sale.*—The contract quoted provides that the seller at his own expense will execute and acknowledge a deed conveying a fee simple title to the purchaser in accordance with the terms of the contract. The deed is to be the statutory short form of the full covenant and warranty deed—that is to say, the form prescribed by statute, by which the instrument is reduced to a simple form of words. Just what such a form contains we shall see when we come to the chapter on "Deeds." It is sufficient to remark here that many sellers, especially those acting in a representative capacity, will not give a warranty deed and the contract may then provide for a bargain and sale deed, or it may state that vendor being a trustee, he will give no covenants or only the usual trustee covenants. This, however, needs to be mentioned in the contract or they do not pass. Both forms of deeds convey the same title, but the full covenant and warranty deed in addition contains certain warranties we shall discuss later.

26. *Personal property included in sale.*—Certain articles of personal property used in connection with the real estate are usually included in the sale. In

the case of an apartment house these are, for example, shades, carpets, gas stoves, janitor's tools, etc. They are part of the property, as a building in actual use, and ought by right to go to a purchaser, altho they are not strictly a part of the realty.

27. *Earnest money a lien.*—In order to protect the purchaser to the extent of the money he pays on the contract, it is provided that such payment and the reasonable expenses of examining the title shall be a lien on the premises. That is, he can look to the property, or the seller's interest in it for the return of these amounts if the contract is not carried out. It is further provided, however, that this lien does not continue if the purchaser should default in his agreement to buy the property.

28. *Risk of damage by fire.*—When the deed is delivered, the purchaser is entitled to get a building, or buildings, in practically the same state as when the contract was signed. It may be held that the purchaser's interest was such that he could insure, and that he ought to take the title even though the building had been damaged by fire during the interim. In order to protect the buyer against such a claim, the wording of the contract places the risk of loss on the seller.

If the subject of the sale is a piece of land the value of which is large compared to the buildings on it, there may be a provision that the title shall pass even tho the buildings be damaged by fire, but that the seller shall turn over to the buyer any amounts he may have collected from fire insurance companies to cover the

loss. It may also be that the value of the buildings is so comparatively small that the fire risk is not considered at all, or the contract may provide that the vendee shall be entitled to the benefit of the existing fire insurance on the premises.

29. *Contract binding on heirs or executors.*—The seller or purchaser may die between the time of making the contract and of closing the title. If the seller dies, his heirs or executors are obliged to carry out the contract. If the purchaser dies, his executors or administrators should pay the purchase price. Either party may assign his interest in the contract. If the seller conveys the land to a third person who knows of the contract, that person would have to carry it out. If the purchaser assigns his contract another principle applies, i.e., a person can assign his rights but not his liabilities. The assignee could pay the purchase price and get the title, but he could not be compelled to do so unless he had expressly assumed the obligation.

30. *Signature, seal, witness and acknowledgment.*—The contract should be signed, sealed and witnessed, but it *need not be acknowledged.* The signatures of both parties are necessary in order that each may hold the other, for the contract cannot be enforced against one who has not signed it. The parties need not sign the same copy, but may sign counterparts.

Seals are important for three reasons: (1) a seal imports consideration, and the burden of proof is on the one who attacks the instrument alleging lack of

consideration; (2) an undisclosed principal cannot be held, since only the one signing a sealed instrument is liable under it; (3) the statute of limitations in New York State is twenty years on a sealed instrument, but only six years on one unsealed and a similar proportion exists in most states.

The contract should be witnessed merely in order to prove the signatures of those whose names are subscribed. Acknowledgments are added to instruments in order that they may be recorded, but as contracts are not usually recorded, they are not usually acknowledged.

REVIEW

A contract for the sale of land by A and B is executed and recorded. Who is the legal owner of the land? What rights has the other party to the contract?

X buys a mill. The owner of the mill property has always enjoyed the privilege of overflowing his pond on the adjacent property. X floods some of his neighbor's land. The neighbor objects. What rights, if any, has X?

In selling a property subject to a mortgage how may the purchaser be required to assume personal liability for the debt?

In a transfer of real property when purchase money mortgage is to be given, who pays for drawing the deed? Who for the bond and mortgage? Who for the search?

X and Y enter into a contract whereby X agrees to purchase Y's house. X assigns his contract to Z. Z refuses to carry out the contract. What may Y do?

Must a contract for the sale of land be in writing?

CHAPTER V

CONTRACTS—EXCHANGES AND AUCTION SALES

1. *Exchange contracts.*—A special form of contract is used for transactions involving an exchange of properties. Land may be exchanged for land, or a parcel of land may be taken in part payment for other land. Owners may wish to get rid of their equities in large holdings and will take free and clear property in exchange, or a man owning a small parcel may offer it as part payment for something more valuable. There are brokers and operators who make a specialty of exchange transactions. A standard form of exchange contract follows:

AGREEMENT, made and dated between

hereinafter described as party of the first part, and

hereinafter described as party of the second part, for the exchange of real property.

Witness, as follows:

The party of the first part, in consideration of one dollar, the receipt of which is hereby acknowledged, and of the conveyance by the party of the second part hereinafter agreed to be made, hereby agrees to sell, grant and convey to the party of the second part, at a valuation, for the purpose of this contract of

Dollars,

All that land with the buildings and improvements thereon in the

The premises which are to be conveyed by the party of the first part shall be conveyed subject to the following encumbrances:

The party of the second part, in consideration of one dollar, the receipt of which is hereby acknowledged, and of the conveyance by the party of the first part hereinbefore agreed to be made, hereby agrees to sell, grant and convey to the party of the first part, for the purpose of this contract, at a valuation of

Dollars,

All that land with the buildings and improvements thereon in the

The premises which are to be conveyed by the party of the second part shall be conveyed subject to the following encumbrances:

The difference between the values of the respective premises, over and above encumbrances, for the purpose of this contract, shall be deemed to be

Dollars, and that sum shall be due and payable as follows, by the party of the

The deeds shall be delivered and exchanged at the office of

at o'clock on 19 .

It is agreed by the respective parties hereto that

brought about this exchange and that the brokerage shall be paid as follows:

Rents and interest on mortgages, if any, are to be ap-

portioned, and the risk of loss or damage to the premises by fire, until the delivery of the deeds, is to be borne by the respective sellers.

If there be water meters on the premises, the respective sellers shall furnish readings to dates not more than thirty days prior to the time herein set for closing title and the unfixed meter charges for the intervening time shall be apportioned on the basis of such last readings.

All personal property appurtenant to or used in the operation of said premises is represented to be owned by the respective sellers and is included in this exchange.

This contract covers all right, title and interest of the respective sellers, of, in and to any lands lying in the bed of any street, road or avenue, opened or proposed, in front of or adjoining the premises to be conveyed to the centre line thereof, or all right, title and interest of the respective sellers in and to any awards made or to be made in lieu thereof, and the sellers will execute and deliver to the purchasers, on closing of title, or thereafter, on demand, all proper instruments for the conveyance of such title and the assignment and collection of such awards.

Each of the parties agrees to convey the property hereinbefore described as sold by such party respectively, free from all encumbrances, except as above specified, and to execute, acknowledge and deliver to the other party, or to the assigns of the other party, a deed in proper statutory short form for record, containing the usual full covenants and warranty, so as to convey to the grantee the fee simple of said premises free from all encumbrances except as herein stated. The deed, in each case, shall be drawn at the cost of the party of the first part thereto.

The stipulations aforesaid are to apply to and bind the heirs, executors, administrators, successors and assigns of the respective parties.

WITNESS the signatures and seals of the above parties.

IN PRESENCE OF { [L. S.]
[L. S.]
[L. S.]

Each party to the contract is at the same time a buyer and a seller. The consideration is the agreement of each party to sell and convey his property in exchange for that of the other party.

2. *Description of the properties.*—There are of course two descriptions. They should be written out in accordance with the principles governing sales contracts. The limitations and encumbrances on each parcel follow the description. Here should be set forth tenancies, restrictions, easements and encroachments as in the sales contract, and in addition the mortgage encumbrances, subject to which the land is to be conveyed.

3. *Financial statement.*—In connection with each parcel, there is a statement that it will be sold and conveyed "at a valuation for the purpose of this contract of ———— Dollars." This amount is stated as the valuation, not the price. Following the description of the property to be conveyed by the party of the second part and encumbrances against it, is the further statement, "The difference between the values of the respective premises over and above encumbrances, for the purpose of this contract shall be deemed to be ——— Dollars." That is to say, taking each property at its given valuation, and deducting encumbrances, there is a difference to be settled by some kind of a payment from one to the other. This figure can be considered as the difference in the agreed values of the equities. The contract then

states which party pays the difference and the manner in which it shall be paid.

The values stated in a contract of this kind are frequently inflated values. As both sides know what land is being transferred the *difference* is the only important figure and no one is deceived. Sometimes merely nominal valuations for each parcel are given, the differences being stated in the same manner as when full or inflated values are given.

4. *Non-performance of contracts.*—The purchaser has the choice of three remedies in case the seller fails to carry out the contract. He may (1) require the return of the earnest money he has paid together with the expenses which he has actually incurred in the examination of the title; (2) sue for specific performance of the contract; or (3) sue for the return of his earnest money and any damages which he can prove that he has sustained by the seller's refusal to complete the transaction. The suit for specific performance is brought when the purchaser can show that he requires the particular property covered by the contract. Here money damages will not compensate him. The property itself is necessary. If the court grant a judgment for specific performance, the seller must comply or he will be guilty of contempt of court. A suit for damages, in which a money judgment is asked, must show that the purchaser has sustained an actual loss by not obtaining the property. If he can prove by expert testimony that the property has a market value in excess of the

price he was to pay for it, this difference would be the measure of his damages. He might also show that he had an opportunity to resell at a profit. Merely prospective or speculative profits, however, would not be a measure of damage.

The seller also has the choice of three remedies if the purchaser fails to complete the contract. He may (1) keep the earnest money and disaffirm the contract; (2) sue for specific performance; or (3) sue for damages. In asking for a judgment of specific performances, he would allege that the buyer was able to pay the purchase price but would not. In suing for damages the seller would try to prove that the purchaser had agreed to pay a certain price, and that the market value of the property was now less than that amount, the difference representing his damages.

The remedies of the parties for non-performance apply both to sales and exchange contracts.

In Canada the courts have wide powers to relieve against penalties and forfeitures. The Judicial Committee of the Privy Council went to considerable length in relieving against a penalty in the case of Kilmer vs. British Columbia Orchard Lands Ltd., L. R. 1913, Appeal Cases 319. There it was stated to be an extremely clear case of a mere penalty for non-payment of the purchase money, from which penalty the company was entitled to be relieved on payment of the balance of the purchase money.

Since August, 1915, several provinces have enacted

what is commonly known as Moratorium Acts. They provide usually that without leave of the court, vendors or mortgagees cannot enforce payment of principal during the war if interest, taxes and insurance are kept paid.

5. *Real estate auction sales.*—Sales of real estate are frequently accomplished by means of public auctions. The sale is advertised and at the appointed time and place the property is offered for sale to the highest bidder. These sales are sometimes voluntary sales held with the consent of the owner, or they may take place against the owner's will. As an agreement is signed when the sale takes place, we may consider them under the heading of contracts.

6. *Involuntary sales.*—While involuntary auction sales are held against the will of the owner of the property, they are the result of some past act on his part, which resulted in creating a debt or obligation. In default of the payment of this debt, the sale of the debtor's property can be required. Preceding such involuntary sales the relation of debtor and creditor, leading to a lien on the real estate, must have existed.

Sales under this heading include sales under the powers of sale contained in the mortgage, mortgage foreclosures, sheriffs' sales under execution of judgments, sales by trustees in bankruptcy, etc. Except the first, they are held under the direction of an officer of the courts, as a referee in a foreclosure action, the sheriff or the trustee in bankruptcy. Frequently a

professional auctioneer is employed to conduct the sale and secure bids on the property offered.

The courts require that such sales be free and unrestricted. An opportunity to buy must be given to everyone present. The interests of an unfortunate owner are being sold out, and those who conduct the sale under authority of the courts, should seek to obtain as much as possible for the property.

7. *Terms of the sale.*—The auctioneer reads a copy of the advertisement of the sale which includes the description of the property. Then he reads the terms of sale, a form of which is given below:

_____
_____ } TERMS OF SALE
_____

The premises described in the annexed advertisement of sale, will be sold under the direction of..... Referee, upon the following terms:

Dated,.....191

1st.—Ten per cent of the purchase money of said premises will be required to be paid to the said Referee, at the time and place of sale, and for which the Referee's receipt will be given.

2nd.—The residue of said purchase money will be required to be paid to the said Referee at his office, No..... in the Borough of.....City of New York, on or before the.....day of .....191 at.....o'clock M., when the said Referee's deed will be ready for delivery.

3rd.—The Referee is not required to send any notice to the purchaser; and, if he neglects to call at the time and place above specified to receive his deed, he will be

charged with interest thereafter on the whole amount of his purchase, unless the referee shall deem it proper to extend the time for the completion of said purchase.

4th.—All taxes, assessments and water rates duly confirmed and payable which, at this date, are liens or encumbrances upon said premises, will be allowed by the Referee out of the purchase money, provided the purchaser shall, previous to the delivery of the deed, produce to the Referee proof of such liens, and duplicate receipts for the payment thereof.

5th.—The purchaser of said premises or any portion thereof, will, at the time and place of sale sign a memorandum of his purchase and an agreement to comply with the terms and conditions of sale herein contained, and pay, in addition to the purchase money, the auctioneer's fee of fifteen dollars for each parcel sold and the salesroom fee of two dollars for each knock down.

6th.—The biddings will be kept open after the property is struck down; and in case any purchaser shall fail to comply with any of the above conditions of sale, the premises so struck down to him will be again put up for sale, under the direction of said Referee, under these same terms of sale, without application to the Court, unless the Plaintiff's Attorney shall elect to make such application; and such purchaser will be held liable for any deficiency there may be between the sums for which said premises shall be struck down upon the sale and that for which they may be purchased on the re-sale, and also for any costs or expenses occurring on such re-sale.

7th.—.....

.....

.....

.....

.....

.....

.....Referee.

MEMORANDUM OF SALE

.....have this.....day of.....191
purchased the premises described in the above annexed printed advertisement of sale, for the sum of.....
.....dollars
.....
and hereby promise and agree to comply with the terms and conditions of the sale of said premises, as above mentioned and set forth.

.....
Address.....
.....191 Received from.....
the sum of.....dollars, being ten per cent on the amount bid by.....for property sold by me under the order in the cause. $.....[1]

The terms stated require the payment of ten per cent earnest money. The third and sixth clause state what happens when default is made by the purchaser. The fourth clause states that any existing liens at the time of sale, such as taxes, assessments and water rates, shall be allowed by the referee out of the purchase money. Following the sixth clause is a space to be used for particulars of any limitations on the title. If the sale is subject to the lien of a prior mortgage, or subject to existing covenants and restrictions, this should be stated. When the sale is of the entire fee of the premises, as in the case of named (usually twenty days later), when the referee purchase price be paid to the referee at the time and place of sale, and that the balance of the purchase price shall be paid at the referee's office on a date

[1] This Receipt is to be returned on the delivery of the deed.

a mortgage foreclosure, any limitations or encumbrances that remain should be stated with as much care as in a contract of sale.

The property is struck down to the highest bidder, who signs the memorandum at the bottom of the terms of sale. He receives a copy containing a receipt by the referee for the payment of 10 per cent of the amount bid.

8. *Voluntary sales by auction.*—The voluntary auction sale has more of the elements of a contract than an involuntary sale. Some voluntary sales are held by trustees, executors, or others acting in a fiduciary capacity; sometimes at their own discretion, and sometimes carrying out the terms of a trust or a will. They may conduct such a sale in order to raise money to pay debts, or to raise money for division among the distributees. Such sales are frequently conducted by owners as a convenient and expeditious means of disposing of real estate. Many large tracts of land are retailed in this manner.

9. *Protected voluntary sales.*—When the sale is held by a trustee, or other fiduciary, it is understood that those who have interests in the proceeds may be present and make bids on the property to protect their interests. When the seller represents his own interests, and reaps all the benefits of the sale, he must either announce and advertise that the sale will be protected, otherwise it must be open, unrestricted and unprotected. It is not fair to bidders to protect a sale which has been advertised as unrestricted, and if one

finds that he has been led to raise his bid thru the efforts of by-bidders or "boosters" he will be relieved of his contract, and can demand the return of his deposit. The seller must keep faith with those whom he has attracted to his sale, and cannot resort to fraudulent practices to gain higher prices. If the seller intends to protect the sale, he must announce it in advance. If he does not, and the prices bid do not suit him, he should withdraw the sale.

10. *Terms of sale in voluntary auctions.*—The terms of voluntary sale are similar to those used for an involuntary sale except that 10 per cent of the accepted bid is paid to the owner, the owner's attorney or the auctioneer. If the auctioneer receives it, he is constituted the agent of the owner for that purpose. The auctioneer's receipt for this 10 per cent is usually required to be surrendered when the deed is delivered. Rents, interest on mortgages and fire insurance premiums are adjusted on a voluntary sale, while they are not at an involuntary one.

11. *Successful auction sales.*—Usually no effort is made to interest the public in an involuntary sale. It is a perfunctory affair, the rights of the parties interested being adjusted by the sale. With a voluntary sale, the principal thing is to attract bidders. This is done by extensive advertising. Successful auctioneers are persistent advertisers. The property and its advantages are brought before the people with reminders of the opportunities presented. Having attracted a crowd to the sale, the auctioneer's skill

and personality are shown in the manner in which he draws out the bids.

REVIEW

If a man wishes to give one parcel of land for another, into what kind of contract will he enter? In this contract is the given valuation the real value? How is the amount paid by one of the parties decided?

What three remedies has the purchaser if the seller breaks the contract? What three remedies has the seller if the purchaser fails? Do these remedies apply to exchange contracts?

Why are auction sales considered as contracts?

What kinds of sales are included in involuntary auction sales? How are they held, and what are their terms?

Who may hold a voluntary auction sale? Distinguish between protected and unrestricted sales.

What difference is there in the terms of sale of voluntary and involuntary auctions?

Of what value is advertising in auction sales?

CHAPTER VI

DEEDS

1. *Forms of deeds in general use.*—The instrument by which immediate title to land is transferred is called a deed. There are three forms of deeds in general use, known respectively as bargain and sale deed, full covenant and warranty deed, and quit claim deed. The law does not require that a deed be worded in any particular manner, but a statute has been enacted in New York giving a short form of deed containing all necessary elements clearly expressed. The statutory short form of bargain and sale deed follows:

THIS INDENTURE, made the day of
in the year nineteen hundred and
BETWEEN.....party of the
first part and——.....——party of the second part:
WITNESSETH, that the said party of the first part, in consideration of the sum of

dollar lawful money of the United States, paid by the said party of the second part do hereby grant and release unto the said party of the second part,
heirs and assigns forever, ALL

TOGETHER with the appurtenances and all the estate and

rights of the party of the first part in and to said premises.

To Have and to Hold the above granted premises unto the said party of the second part,
heirs and assigns forever.

In Witness Whereof, the said party of the first part has hereunto set hand and seal the day and year first above written.

In the presence of

STATE OF NEW YORK, COUNTY OF ss.:
On this day of , in the year

nineteen hundred and , before me, came

to me known to be the individual described in, who executed the foregoing instrument, and acknowledged that he executed the same.

This deed contains the substance of bargain and sale deeds in use in most jurisdictions and the comments made apply equally to them.

2. *Indenture, date and parties.*—The expression "this indenture" is a relic of the ancient custom of preparing instruments in duplicate on the same sheet, and then tearing them apart. The ragged edges or indentations when brought together helped to prove that the instrument was authentic. Formal instruments are now frequently called indentures.

The date is not essential to a deed but is merely a convenient memorandum. If nothing can be found

to the contrary it is assumed that the deed was executed and delivered on the day of its date.

The parties in the deed reproduced are designated as party of the first part and party of the second part. The parties are usually known as "grantor" and "grantee." The grantor should, of course, be a person considered as fully competent of entering into a formal contract.

3. *Consideration.*—There is no legal necessity for making reference in the deed to the consideration given for the conveyance, but it is advisable to do so, as the burden of proving that no consideration was given then passes to anyone attacking the instrument. While the full purchase price may be stated if the parties wish it, frequently the consideration stated is merely nominal; that is, it may be mentioned as "one dollar" or "one dollar and other valuable considerations" or "one hundred dollars and other valuable considerations."

In dealing with fiduciaries, it is important that the full consideration be stated in the deed, since fiduciaries are generally without authority to convey property committed to their charge, except for a valuable consideration, usually money. If, for some reason, it is not desired to make public the amount of consideration paid, an agreement regarding it, or a receipt for its payment, executed by the fiduciary in recordable form, should be obtained. If at any time the title is questioned because the deed does not set forth the consideration, the separate instrument

showing the payment may be recorded in support of it.

The consideration for a transfer of real property may be either a good or a valuable consideration. A consideration is termed good when the transfer is made because of blood relationship or because of natural affection. Such relationship or affection is recognized by law as sufficient consideration to support the transfer of property to another without the passing of anything of value. Such a conveyance is not good against creditors whose claims are in existence and valid at the time of the transfer.

A valuable consideration may be a transfer of money or of anything of value. It may consist either in some right, interest, profit or benefit accruing to the one party, or some forbearance, detriment, loss or responsibility given, suffered or undertaken by the other. Marriage is a valuable consideration under English law. It may also be a change either actual or potential in the financial position of one in favor of another. Any deed made without valuable consideration (even tho the one were inserted fictitiously) may be set aside by creditors as a fraud upon their rights. Creditors, whose claims arise after the conveyance, have no ground for attacking the transfer.

A deed may be void when the consideration is illegal or against public policy or when induced by fraud or duress.

4. *Granting clause.*—"Does hereby grant and release unto the said party of the second part, his heirs

and assigns forever"—these words, known as the granting clause are important. By this clause the title is transferred from one party to the other. The language used is similar to that employed for the conveyance of an estate in fee simple. If any less estate than a fee is to be transferred by the deed, the language of the clause should be changed appropriately. For example, if a life estate were to be granted, the wording would be "does hereby grant and release unto the said party of the second part for and during the term of his natural life."

5. *Description of property transferred.*—The description of property to be included in a deed should be more detailed than in a contract. It should be quite definite and easily traced because it is permanent. The contract lasts for only a short time, but the deed is usually recorded and becomes part of the permanent history of the title to the land. The deed affects not only the present parties, but also their successors in ownership.

Two methods of description are employed in deeds: one by metes and bounds, the other by references to maps or monuments. The following is a specimen of a description by metes and bounds:

> All that certain plot, piece, or parcel of land situate, lying and being in the Borough of Manhattan, City and State of New York, bounded and described as follows: —Beginning at a point on the northerly side of Thirty-fourth street, distant eighty-five feet westerly from the corner formed by the intersection of the northerly side of Thirty-fourth Street with the westerly side of Fifth

> Avenue; running thence northerly parallel with Fifth Avenue one hundred feet; thence westerly parallel with Thirty-fourth Street fifty feet; thence southerly again parallel with Fifth Avenue, one hundred feet to the northerly side of Thirty-fourth Street and then easterly along said side of Thirty-fourth Street fifty feet to the point or place of beginning.

From this description the location of the property can be ascertained with exactness. A definite point of beginning is determined, i.e., a point on the northerly side of Thirty-fourth Street, eighty-five feet westerly from the northwesterly corner of Thirty-fourth Street and Fifth Avenue. From that point the description proceeds by metes (measures) and bounds (directions) around the entire plot. The measures are exact and the directions are absolutely fixed. A description like this is of course the most satisfactory. The example given is a very simple one; in some cases a metes and bounds description may be used for a farm or a tract of land of many acres. The directions and distances may then be stated with reference to the point of the compass as, "north five degrees six minutes west, 857 feet."

A description by reference to a map may be used when the property is part of a tract that has been mapped, as—

> Lots one to ten inclusive in Block 76 on map of Jones Estate, made by George Edwards, Civil Engineer and Surveyor, filed in the Office of the Clerk of Albany County, on February 11, 1893.

Such a description conveys the land as it is shown

on the map to which reference is made. The map is usually, but not always, filed as part of the public records.

A description by monuments is one which not only depends on metes and bounds, but is controlled by natural monuments and cannot be ascertained except by a knowledge of matters of geography or topography outside the recorded description. A description which reads:

> Beginning on the side of the road running from Westchester to Yonkers, at the northwest corner of the farm of John Smith, and thence southerly along John Smith's farm to a rock at the corner of Jones's farm, and thence westerly along Jones's farm to a blazed tree at Robinson's barn, etc.,

is a description which depends for its identity entirely upon matters outside the record title to the property. It is controlled not by the distances stated, but by the natural monuments. Descriptions of this sort are frequent, and if the property can be identified and the natural monuments on the ground can be found, it is sufficient. One hundred years from now it may be troublesome to construe such a description and in order to identify a tract it may be necessary to examine the title to all the surrounding property, and make surveys and topographical maps of all the surroundings. However, if it can be ascertained in any dependable way in accordance with all known methods which an engineer may suggest, what was the subject of that conveyance, it is valid, and will convey the property described.

A description which is absolute in its metes and bounds is the one extreme; a description which depends entirely upon monuments, natural or artificial, is the other extreme. Between these there are many descriptions which partake of the character of both.

Reference to other conveyances or to some map helps to identify the property to be conveyed; after a description by metes and bounds, the deed may state that it is the property which was conveyed to the seller by a certain deed, citing it by its parties, its date and place of record. Then if a mistake has been made in copying the description from the other deed, the mistake will correct itself by the reference to the deed mentioned.

6. *Uncertain, ambiguous and inconsistent descriptions.*—Any description by which the property may be identified is good, but an uncertain description which renders the property incapable of identification makes the instrument void. If a description is merely ambiguous, it does not follow that it is so uncertain as to be void. In the attempt to support the transaction it is only fair that reference should be made to matters outside the instrument itself which will result in the identification of the subject matter. Again, there may be several elements in the description in the deed which are inconsistent in themselves. In such a case it would be pertinent to inquire into the real intent of the parties.

An example of an uncertain description is "one of several houses owned by the party of the first part in

the Borough of Brooklyn"; of an ambiguous description, "the most easterly of five lots fronting on Grand Street owned by the party of the first part"; of an inconsistent description, "lot 5 in Block 68 on Map B, described as" (metes and bounds description here inserted being of a lot in an entirely different block).

A deed that is not ambiguous on its face must be construed by itself. Regardless of the intentions of the parties, or any misunderstandings between them, outside parties can rely on the record and be secure against any claims the parties to the deed may make regarding it. There is a distinct line between latent ambiguity and patent ambiguity.

7. *Appurtenances.*—The clause "with the appurtenances, etc." follows the description. Appurtenances are rights which go with the land, altho not mentioned in the description. They include such things as the right to maintain a wall on another man's land, or the right to cross other property to reach a highway. As a matter of legal construction appurtenances go with the land whether specifically conveyed or not.

8. *Habendum.*—"To have and to hold the above granted premises unto the said party of the second part his heirs and assigns forever." This part of the deed is known as the habendum. It should contain a clear expression of what is intended to be conveyed by the instrument. The language quoted is that used for the transfer of an estate in fee simple. If any other estate is to be granted, it should be stated

clearly, not only in the granting clause but also in the habendum clause. A conveyance upon trust, for example, would be worded: "To have and to hold the above granted premises unto the party of the second part, his successors and assigns forever, upon trust however to and for the following uses," after which the conditions of the trust are set forth.

9. *Conveyance subject to incumbrance.*—Property is often conveyed subject to a mortgage which is a lien upon it. This may be covered by inserting after the habendum a clause such as, "Subject however to the lien of a certain indenture of mortgage made for $5,000 and interest." Rights of tenants, easements, restrictions, etc., affecting the property should also be stated in the deed in a similar manner.

If restrictions are being imposed upon the property at the time of the conveyance, they are usually inserted in the deed by a clause such as the following: "The said party of the second part does hereby covenant and agree to and with the said party of the first part as follows": (here follows the exact wording of the restriction agreed upon.)

10. *Testimony clause, signature and seal.*—The testimony clause just before the place for the signature is purely formal. The deed would be just as good without it. The signature of the party of the first part is usually the only one which appears on the deed. It may be the ordinary writing of the name or it may be just a mark. Anything made by

the grantor and intended for his signature is sufficient.

In many states it is necessary that the deed be sealed. In the State of New York deeds by individuals need not have a seal. It is to the advantage of the grantee, however, that for two of the reasons noted in our chapter on contracts a seal be affixed; first, consideration is imported by the seal, second, the time of the statute of limitations is longer on a sealed instrument. In Canada deeds require seals, but transfers under Land Titles Acts do not.

11. *Execution by corporation.*—A deed made by a corporation is executed by the signature of one or more officers acting on its behalf, and by affixing the corporate seal. Frequently, the name of the corporation is written above the signature of the officers, but this is not necessary tho it is preferable. The seal, however, is a necessary part of the execution. It usually consists of an impression made upon the paper, and frequently takes the form of two concentric circles, with the name of the corporation between them. There are a few corporations which have not adopted a corporate seal. When such a corporation executes a deed, the individual seals of the persons attesting the instrument are attached.

12. *Acknowledgments.*—Practically every deed whether by an individual or a corporation is acknowledged or proved before officers authorized to take acknowledgments. When this has been done the deed

is entitled to be spread upon the public records. A corporate deed is usually proved by the officer who signed it. The form of individual acknowledgment appears at the bottom of the deed reproduced in this chapter. The form of certificate for a corporate acknowledgment is as follows:

STATE OF NEW YORK, COUNTY OF NEW YORK, *ss.:*

On this *eighth* day of *January* one thousand nine hundred and *seventeen* before me personally came *John Smith* to me known, who being by me duly sworn, did depose and say that he resides *in the Borough of Manhattan, City of New York;* that he is the *President* of *SMITH REALTY COMPANY*, the corporation described in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by order of the Board of *Directors* of said corporation, and that he signed his name thereto by like order.

13. *Bargain and sale deed with covenants.*—The bargain and sale deed already described conveys just as good a title as any deed can convey. It is appropriate under certain circumstances for the grantor, in addition to conveying the title, to make certain covenants with regard to it. The bargain and sale deed therefore often has added to it covenants known as "covenants against grantor's acts." These covenants have to do only with what has happened to the title during the time the grantor has owned it. The grantor represents that "he has done

or suffered nothing whereby the premises have been encumbered in any manner whatsoever."

This covenant is made usually by persons acting in a fiduciary capacity, sometimes by other individuals, and by some corporations. Fiduciaries cannot be expected to know what happened to the property in the past nor to make warranties as to the future, but they can covenant as to their own doings in relation to it.

14. *Quit-claim deed.*—A quit-claim deed is exactly similar in form to a bargain and sale deed, except that in place of the words "grant and release" the terms used are "remise, release and quit claim." A quit claim deed will convey the entire estate of the grantor in the same manner as a bargain and sale deed, but it is usually employed to release some claim, real or supposed, upon the property.

15. *Full-covenant-and-warranty deed.*—The full covenant and warranty deed is like the bargain and sale deed in form except that five covenants made by the grantor are added to it. These covenants do not help the transfer of the title in any way, but are assurances respecting the title conveyed.

The form of the covenants in New York deeds is as follows:

And the said..... do..covenant with said part..of the second part as follows:

First.—That said..... seized of the said premises in fee simple, and ha..good right right to convey the same..

Second.—That the part..of the second part shall quietly enjoy the said premises.

Third.—That the said premises are free from encumbrances.

Fourth.—That the part. . of the first part will execute or procure any further necessary assurance of the title to said premises.

Fifth.—That the said..... will forever warrant the title to said premises.

16. *Explanation of the five covenants.*—The five covenants contained in the full covenant and warranty deed may be considered in the order in which they appear.

The covenant of seizen. This covenant signifies that the grantor owns the property, possesses it and has a good right to convey it to the grantee.

Covenant of quiet enjoyment, "that the party of the second part shall quietly enjoy the said premises." This means that the grantee shall not be disturbed in his possession of the property by reason of any right or cause of action which existed at the time of delivery of the deed.

Covenant against encumbrances. The grantor covenants that the title to the premises is free from all encumbrances. If any encumbrances exist and it has been agreed that the grantee takes subject to them, they should be set forth in the deed, either after the description or after the habendum. Then the clause will read, "That the said premises are free from encumbrances, *except as aforesaid.*"

Covenant for further assurance. This covenant provides that whenever necessary the grantor will give other instruments to perfect the title of the

grantee. This may be useful in case the deed should prove to be defective in any respect. If the grantor under this deed can remove the defect—whatever it may be—by executing or procuring a further assurance of title, he must do so.

Covenant of warranty. This is the most important of the five covenants. It means an absolute guarantee of the title on the part of the grantor.

17. *Covenants divided into two classes.*—Two of the covenants relate to the past and three relate to the future. Those which relate to the future are said to "run with the land." The two which relate to the past, and which do not run with the land are the covenant of seizen and the covenant against encumbrances. If these two covenants are broken, the breach occurs when the deed is delivered. Subsequent conveyances may operate to assign the cause of action on the breach, but the right of action accrues, and the time of limitation begins to run, at the time of delivery of the deed.

The other three covenants run with the land. They are binding covenants passing with the title to the land until broken, and enforceable by the owner at the time any breach occurs. The time of limitation begins to run, not from the delivery of the deed, but from the date the covenant is broken. After being broken, the covenant no longer runs with the land; the right of action, however, may pass by assignment.

18. *Breach of covenants.*—The covenant of seizen is broken at the time of delivery of the deed if any of

the elements of ownership, possession and right to convey do not exist. The covenant against encumbrances is also broken at that time if encumbrances not mentioned in the deed are in existence against the property. The covenant of quiet enjoyment might not be broken even tho the grantor did not have a title in fee simple absolute. If the fee could be defeated by any contingency, the breach of this covenant would not occur until the grantee or those claiming under him were ousted from the enjoyment of the property. The covenant for further assurance is not broken until the grantor fails to give some other instrument when such action becomes necessary. He can then be sued for specific performance, or for damages after performance has been demanded and refused.

The covenant of warranty cannot be invoked until the owner claiming under it has been actually ousted of his ownership, i.e., deprived of all the land or some essential portion. He can then claim damages under the covenant. The measure of damage is not the value of the land at the time of the breach, but the consideration paid for the conveyance containing the covenant.

There is no obligation on the part of the grantor to make good under any covenant until there is loss or liability thru loss. In some states the rule regarding the covenant against encumbrances is that the mere existence of an encumbrance shall be sufficient to call upon the maker of a covenant to respond. In

New York the rule is more limited—the holder of the covenant must actually buy his way out before he can recover against the covenantor.

19. *Covenants do not guarantee marketability.*—The covenant of warranty is in no manner an assurance that the title to the property conveyed is marketable. There are many ways in which a title may prove unmarketable for which there is no redress upon any covenant in the deed. A house may encroach upon a neighbor's land, and the owner may have no right to maintain it there. If he tries to sell the house, the purchaser may decline to take the title. He will be in possession of an unmarketable title, but he has not been ousted of anything which is within the bounds of the land described in the deed and has not been deprived of any valuable thing which was conveyed to him. Therefore, he has no redress under the covenant of warranty. A building may have an important projection upon a public street, so that the title is unmarketable, and a purchaser would not take it, neither would a lender lend on it, and yet there may be no redress under any covenant. The title may also be unmarketable because of some defect in the chain of title, or because of the possibility of some lien (such as a lien of decedents' debts) being asserted against it. A purchaser might not be compelled to take the title under the circumstances, and yet there would not be a breach of any of the covenants contained in the warranty deed we have analyzed.

REVIEW

What is a deed? Name three forms. How are the parties to a deed designated?

State the distinction between a good and a valuable consideration. Under what circumstances may a deed be invalid even if it recites a proper consideration?

What is meant by the granting clause; habendum clause? How are they modified by circumstance?

Explain what methods of description of the property may be employed in a deed and the merits of each. What is the danger in the description by monuments? How may an ambiguous description be overcome?

Should a deed be sealed? What are the requirements in the execution of a deed by a corporation? How are deeds acknowledged?

State the difference between a bargain and sale deed and a quitclaim deed?

In a warranty deed which covenants are said to "run with the land" and why? What are the covenants of seizen, and against encumbrances?

What redress has the grantee for a breach of the covenants? Does a covenant of warranty assure marketability?

CHAPTER VII

BONDS AND MORTGAGES

1. *Use of the bond and mortgage.*—When real property is given as security for the payment of a debt or obligation, the instrument used for the purpose of transferring the title to such property as security is called a mortgage. The debt itself is usually evidenced by a bond or note. In New York, the principal instrument used in connection with a mortgage is the bond. In some other states it is a note, or a series of notes. Immediate title to land is not transferred by a mortgage. The transfer is merely potential. Possession of the property is usually retained by the mortgagor or his successors.

Before modern method was adopted, the lender got actual ownership together with the right of possession. The borrower retained only a right in equity to redeem his land upon payment of the debt and this interest in the property was known as the *equity of redemption.*[1] Under modern conditions, that term continues to designate the interest of an owner in his land, over and above the interest of the

[1] In England, Canada, and in Massachusetts, New Hampshire, Maine, Illinois, and probably in some other states, the legal title to the land is transferred by the mortgage to the first mortgagee, and the mortgagor retains only on equitable interest or estate in the property—his equity of redemption. A. G. Reeves, "Real Property." Vol. II, page 1,050.

mortgagee. Under the various Land Title Acts in Canada the legal title to the lands is not transferred, but the land is charged with the payment of the mortgage money.

A mortgage is personal property and if taxed, is taxed as personal property. It passes from one holder to another by assignment and delivery and not by deed. Because it is a chattel interest and a lien upon the land and not an immediate transfer of the title, there may be not only a first mortgage but also a second, a third, as many, indeed, as the owner may be able to obtain. Each mortgage takes its rights in the order of precedence, the subordinate or junior being subject to the rights of the senior or prior mortgages.

2. *Form of bond.*—A form of bond in use in New York is as follows:

KNOW ALL MEN BY THESE PRESENTS, That

hereinafter designated as the obligor do hereby acknowledge to be indebted to

hereinafter designated as the obligee , in the sum of

dollars, lawful money of the United States, which sum said obligor do hereby covenant to pay said obligee or assigns, on the.....day of Nineteen Hundred and

with interest thereon, to be computed from the day 1 , at the rate of per centum per annum, and to be paid on the day of next ensuing the date hereof, and semi-annually thereafter.

AND IT IS HEREBY EXPRESSLY AGREED THAT the whole of said principal sum shall become due at the option of said obligee after default in the payment of any interest for thirty days, or after default in the payment of any tax or assessment for thirty days after. All the covenants and agreements made by the said obligor in the mortgage covering premises therein described and collateral hereto, are hereby made part of this instrument.

Signed and sealed this day of , 19 .

IN THE PRESENCE OF

(Note.—On opposite page of this Bond space is provided for the entry of interest payments, and for payments on account of principal.)

3. *Provisions of the bond.*—The bond contains the names of the parties to it, one person or several persons described as obligor, or obligors, acknowledging himself or themselves to be indebted to some other person, or persons, described as obligee, or obligees, for a definite sum in money. The obligor covenants to repay the sum on a definite date as well as interest computed from a given date at an agreed rate and payable at certain fixed times. The last part of the bond contains a reference to the mortgage collateral to it, makes the agreements and covenants in the mortgage part of the bond, and provides that the whole debt may become due at the option of the obligee, upon default in the payment of interest for

thirty days, or upon default in the payment of taxes or assessments upon the mortgaged premises for thirty days. The instrument is dated, signed, sealed and witnessed, and often acknowledged.

If there is more than one obligor, the words "jointly and severally" are inserted in the blank space following the words "to be." The holder of the obligation can then enforce payment of the entire amount against all or any one of the obligors. Each person signing the bond incurs a personal liability for the payment of the whole debt.

Bonds are frequently written for twice the amount of the principal. The amount so fixed is known as the penalty or "penal sum" of the bond. It creates no obligation to pay more than the true amount of the debt. In fact, such a bond will contain a provision that if the real debt and interest is paid, the bond is void. The principal sum in the bond reproduced above is mentioned as being "lawful money of the United States." In some cases, especially when the mortgage secures an issue of bonds to be sold to investors, payment is required to be made in "gold coin."

The principal sum is payable on a definite date. The obligor has no option of prepayment unless the bond specifically provides for payment "on or before" the specified date or contains a special clause to the effect that the obligor has the privilege of paying the sum before maturity. It should be noted, however, that in the usual first mortgage made for

investment of funds the privilege of prepayment is not customary. The lender dictates the terms, and he may wish his money to be placed and drawing interest, so that the investment may not be disturbed. When the privilege of prepayment is granted, provision is often made that interest shall be paid on a date subsequent to the date of payment of the principal. This is not usury, but a price paid for the privilege of paying off the debt before the due date.

The interest should of course be fixed at not more than the legal rate. It is computed from the day stated in the bond (usually the day the bond is dated) and is payable on a fixed date thereafter, and then in regular instalments, usually semi-annually, sometimes quarterly or even monthly. It is not paid in advance. The lender often specifies the interest days desired by him. Some savings banks have a rule that interest on all mortgages held by them be paid on the same interest days.

4. *Default in the payment of interest and taxes.*— The holder of a properly prepared bond has the option of considering the entire principal due if there is any default in the payment of interest for thirty days, or if taxes or assessments on the mortgaged premises remain unpaid for thirty days. This provision protects the lender who has advanced money on the security of the bond and mortgage. Without this provision, in case of default, suit would have to be brought separately on each instalment of interest and the lender would be without power to require the

owner to pay the taxes and assessments on the land. Hence the power contained in this provision adds to the security of the loan. The holder of the bond has, of course, the right to waive any default, and can reinstate the credit even after he has exercised his option. Mere forbearance to take action does not mean a waiver of the default, but if interest or taxes be paid before the option is exercised, the option is considered waived.

5. *Execution and enforcement of the bond.*—Each obligor must execute the bond. It is usually sealed because there are longer legal limitations on a sealed instrument. The statute of limitations begins to run from the due date, or the last time there was an acknowledgment of the obligation—as by payment of interest upon it. A bond need not be witnessed or acknowledged to be enforceable, but it is often both witnessed and acknowledged.

The holder of the bond can enforce it by foreclosing the mortgage which accompanies it, or he may bring suit on the bond. If he sues on the bond, he must exhaust his remedies under that instrument before he can enforce the mortgage, but he may foreclose the mortgage in the first instance, and ask for a judgment against the bondsman for any deficiency that may arise on a sale of the property.

6. *Form of mortgage.*—The bond we have analyzed is an evidence of the debt; the mortgage is given as security for the debt. While there are a number of mortgage forms in general use, the fol-

lowing may be taken as a specimen of what the complete instrument should contain.

THIS INDENTURE, made the day of in the year nineteen hundred and , between

hereinafter described as party of the first part, and

hereinafter described as party of the second part.

WHEREAS, the said

by virtue of a certain bond or obligation bearing even the date herewith, justly indebted to the said party of the second part in the sum of dollars, lawful money of the United States, secured to be paid on the day of in the year nineteen hundred and , together with the interest thereon from the day of 191 , at the rate of per centum per annum, and to be paid on the day of next ensuing the date hereof and semi-annually thereafter.

IT BEING THEREBY EXPRESSLY AGREED that the whole of the said principal sum shall become due after default in the payment of interest, taxes, assessments or water rents as hereinafter provided.

NOW THIS INDENTURE WITNESSETH, that the said party of the first part, for the better securing the payment of the said sum of money mentioned in the said bond or obligation, with interest thereon, and also for and in consideration of one dollar paid by the said party of the second part, the receipt whereof is hereby acknowledged, doth hereby grant and release unto the said party of the second part, and to and assigns, forever, all

(Description of property follows.)

TOGETHER with all fixtures and articles of personal property used in connection with said premises, all of which are declared to be covered by this mortgage.
TOGETHER with the appurtenances and all the estate and rights of the party of the first part, in and to said premises.
TO HAVE TO HOLD the above granted premises unto the said party of the second part,

and assigns forever. PROVIDED ALWAYS, that if the said party of the first part,

or the heirs, executors or administrators of the party of the first part, shall pay unto the said party of the second part,

or assigns, the said sum of money mentioned in the said bond or obligation, and the interest thereon, at the time and in the manner mentioned in the said bond or obligation, that then these presents and the estate hereby granted, shall cease, determine and be void.

AND said party of the first part covenants with the party of the second part as follows:

FIRST. That said party of the first part will pay the indebtedness as hereinbefore provided, and if default be made in the payment of any part thereof, the party of the second part shall have power to sell the premises herein described, according to law. Said premises may be sold in one parcel, any provision of law to the contrary notwithstanding.

SECOND. That the party of the first part will keep the buildings on the said premises insured against loss by fire for the benefit of the party of the second part. Should the party of the second part by reason of such insurance against loss by fire, as aforesaid, receive any sum or sums of money, such amount may be retained and applied by said party of the second part toward payment of the sum hereby secured, or the same may be paid over either wholly or in part to the said party of the first part,

or assigns, to enable said party

of the first part to repair said buildings or to erect new buildings in their place, or for any other purpose or object satisfactory to the said party of the second part, without affecting the lien of this mortgage for the full amount secured thereby before such damage by fire, or such payment over, took place.

THIRD. And it is hereby expressly agreed that the whole of said principal sum shall become due at the option of the holder of this mortgage after default in payment of interest for thirty days, or after default in the payment of any tax or assessment or water rent for thirty days, or upon the failure to exhibit to the holder of this mortgage, on demand, the receipt therefor, or after default for thirty days after notice and demand in the payment of any instalment of any assessments for local improvement heretofore or hereafter laid which is or may become payable in annual instalments, and which has affected, now affects, or hereafter may affect the said premises, notwithstanding that such instalment be not due and payable at the time of such notice and demand, or immediately upon the actual or threatened demolition or removal of any building erected upon said premises, or if for any reason it shall be impossible to obtain fire insurance on the premises covered by this mortgage from fire insurance companies lawfully doing business in the State of New York.

FOURTH. That the holder of this mortgage, in any action to foreclose it, shall be entitled, without notice and without regard to the adequacy of any security for the debt, to the appointment of a receiver of the rents and profits of said premises; and said rents and profits are hereby, in the event of any default or defaults in paying said principal or interest or taxes and assessments, or water rents, assigned to the holder of this mortgage as further security for the payment of said indebtedness.

FIFTH. That until the amount hereby secured is paid, the party of the first part will pay all taxes, assessments and water rents which may be assessed or become a lien on said premises, and, in default thereof, the holder of this mortgage may pay the same, and the party of the first part will repay

the same with interest, and the same shall be a lien on said premises and secured by this mortgage.

SIXTH. In the event of the passage after the date of this mortgage of any law of the State of New York, deducting from the value of land for the purposes of taxation any lien thereon, or changing in any way the laws for the taxation of mortgages or debts secured by mortgage, for State or local purposes, or the manner of the collection of any such taxes, so as to affect this mortgage, the holder of this mortgage, and of the debt which it secures, shall have the right to give thirty days' written notice to the owner of said land requiring the payment of the mortgage debt, and it is hereby agreed that if such notice be given, the said debt shall become due, payable and collectible at the expiration of said thirty days.

SEVENTH. That the mailing and demand of a written notice by depositing it in any post-office, station, or letter box, inclosed in a post-paid envelope addressed to the owner of record of said mortgaged premises and directed to said owner at the last address actually furnished to the holder of this mortgage, or, if no such address has been furnished, then to such record owner at said mortgaged premises, shall be sufficient notice and demand in any case arising under this instrument.

EIGHTH. That the party of the first part will execute any further necessary assurance of the title to said premises, and will forever warrant said title.

NINTH. The party of the first part, or any subsequent owner of the premises described herein, shall, upon request, made either personally or by mail, certify, by a writing duly acknowledged, to the party of the second part or to any proposed assignee of this mortgage, the amount of principal and interest then owing on this mortgage; upon failure to furnish such certificate after the expiration of six days in case the request is made personally, or after the expiration of thirty days after the mailing of such request in case the request is made by mail, this mortgage shall become due at the option of the holder thereof.

IN WITNESS WHEREOF, said party of the first part has signed
the day and year first above written.

7. *Parties to the mortgage.*—The party of the first part is the owner of the property, and is often referred to as the mortgagor. The party of the second part is the person to whom the debt is payable, the lender or the representative of the lender, usually called the mortgagee. It is customary that the wife of the owner join in the mortgage in order that it may be a lien superior to her dower rights. The security is defective unless she does bar her dower, where by law she would be entitled to dower. In the Province of Ontario, Nova Scotia, New Brunswick, Prince Edward Island, a wife is entitled to dower and in British Columbia to a limited extent. It is not necessary that the wife join in the bond.

8. *Recital of the obligation.*—Immediately after the names of the parties there is a reference to the debt which the mortgage is made to secure. A blank space is left in which to insert the name of the maker of the bond. As a general rule, he is the same person as the maker of the mortgage, but in some cases a mortgage is made to secure the debt of a third party, as, for example where a wife mortgages her property to secure her husband's indebtedness. The bond is described as "bearing even date herewith." It is usual and customary that both bond and mortgage be dated alike, yet there is no reason why a mortgage should not be given to secure an antecedent debt.

The due date of the principal sum, the rate of interest and the times when the interest is payable are stated. In the next paragraph provision is made that upon default in the payment of interest, taxes or assessments, the whole principal sum may become due.

9. *Mortgaged premises.*—The premises in question should be described in the mortgage as carefully as they would be in a deed. The granting clause and the habendum follow the language of the deed. It is stipulated, however, that the conveyance is made to furnish better security for the payment of the principal sum and interest.

Immediately following the description of the property is a clause whereby the mortgage is made to cover all fixtures and articles of personal property attached to, or used in connection with the premises described. This clause is intended to bring under the lien of the mortgage such articles upon the premises as may not be real property, or which may be claimed to be personalty, such as gas ranges or lighting fixtures. This clause does not of course bring household furniture under the mortgage but makes it cover all that is essentially a part of the property and necessary for its use.

10. *Defeasance clause.*—If the instrument ended here, it would be very similar to a deed. What is known as the defeasance clause, however, makes it a mortgage. This provides that if the amount of the bond and interest is paid "at the time and in the man-

ner mentioned in the said bond or obligation, that then these presents and the estate hereby granted shall cease, determine and be void."

In some states it is necessary that the defeasance clause be recorded at the same time as the instrument which creates the lien. If it is not so recorded, the mortgagee can take no advantage from recording the conveyance. The law seeks to prevent, as far as possible, any hidden conditions of this sort.

The mortgage being personal property, the defeasance clause provides that payment shall be made to the party of the second part, his personal representatives or assigns. The conveyance of the land, however, which follows the language of the deed, is to the party of the second part, his heirs and assigns.

With the defeasance clause included, nothing more is needed to make the instrument a complete and legal mortgage. It is a conveyance of land upon security, the transfer being defeated by the payment of the obligation. The lender, however, requires further and additional safeguards, and for his benefit a number of covenants and agreements are inserted.

11. *Property to be sold as a whole.*—The first covenant is a repetition of the obligation in the bond, a promise by the party of the first part to pay the indebtedness. It also contains a stipulation that if any default occurs, the party of the second part shall have power to sell the property according to law. To protect the borrower the law requires that in order to execute the power of sale conferred on the mortgagee

by this covenant, the mortgage be foreclosed. In some jurisdictions the mortgage gives a power of sale without the necessity of resorting to the courts.

The last sentence of this covenant provides that the premises may be sold in one parcel, regardless of any provision of law to the contrary. The lender may consider the property more valuable since it is held in single ownership, and consequently better security for the loan if it can be sold as one parcel under foreclosure. The general rule of law requires that when the property can be divided into separate lots forming natural divisions, such lots must be offered for sale separately and only so much of the property sold as will satisfy the claim of the mortgagee. If an owner is being foreclosed by legal action, and he can show the court that it would be a hardship upon him to have the property sold as one tract, the court may grant relief from this stipulation and order the property to be sold in separate parcels. This is usually done with the provision that if this method of sale does not raise enough money to pay off the mortgage, the property may then be offered for sale in one parcel.

12. *Insurance to be maintained.*—The second covenant provides that the owner will keep the buildings on the premises insured for the benefit of the mortgagee against loss by fire. Often the buildings are a more important part of the security for the loan than the land. Loans on improved property are usually made for a larger proportion of the value of

the property and at a lower interest rate than loans on unimproved property. It is therefore extremely important that the mortgagee have insurance policies in his possession, protecting him against loss arising thru damage to the buildings by fire. Such policies are made out in the name of the owner, but with a rider attached making any possible loss payable to the mortgagee, as his interest may appear. The original policy is retained by the mortgagee and the owner is furnished with a copy by the insurance company.

The latter part of the second covenant provides what shall be done with the insurance money collected by reason of any fire loss. The proceeds may be applied by the mortgagee toward the payment of the debt. The money may be paid over to the owner in whole or in part, to enable him to repair the buildings or erect new ones in their place, or it may be used for any other purpose satisfactory to the mortgagee. Payments by insurance companies do not affect the lien of the mortgage for the full amount.

13. *When the mortgage becomes immediately payable.*—The third covenant states the circumstances under which the whole of the principal sum of the mortgage and interest becomes due and payable prior to the agreed date. This may be on account of nonpayment of interest, taxes or assessments, or by reason of actual or threatened demolition or removal of the buildings on the premises. The covenant does not say that thirty days grace shall be allowed for the

payment of interest, but it does say that if the interest remains unpaid for thirty days the mortgagee can not only enforce payment of the interest in arrears, but can require payment of the principal as well. Were it not for this agreement, suit could be brought for the unpaid interest only. The mortgagee is also given the option of calling for payment of the mortgage if taxes or assessments remain unpaid for thirty days. As taxes and assessments create a lien which takes precedence of the mortgage, the security of the mortgage lien is impaired when they are not paid. The mortgagee need not extend further credit under such unfavorable circumstances.

The buildings on the premises are under the control of the owner. They are very often an important part of the security. Under this clause the mortgagee can require payment of his mortgage if the owner threatens to destroy or remove the buildings, or if he actually has accomplished their destruction or removal. If he knows such action is threatened he can obtain an injunction, restraining the owner from committing waste.

Any new building placed upon the land becomes realty and comes under the lien of the mortgage. The mortgage attaches to all that is realty as long as the lien continues.

14. *Appointment of a receiver.*—The fourth covenant provides that if an action of foreclosure is brought, the mortgagee shall be entitled to the appointment of a receiver for the rents and profits of

the property. Under this clause no notice need be given of the application for the appointment of the receiver, and the right is given regardless of whether the property is sufficient security for the debt or not. It happens frequently that when it is necessary to foreclose, the land and buildings are not adequate security for the amount owing. This is so especially if the amount of unpaid taxes and interest is large. The appointment of a receiver gives added security to the mortgagee, as in the event of a deficiency at the foreclosure sale, the surplus in the receiver's hands, less commissions, will be applied to the payment of the mortgage.

The court may decline to appoint a receiver, even when the mortgage contains a receivership clause, if the court deems it unnecessary to do so. Similarly, they may appoint a receiver during foreclosure upon proper application and due notice, even tho the mortgage contained no such privilege.

This covenant also proceeds to pledge the rents and profits as further security for the debt in the event of default. The intent of this is to give the mortgagee the right to exercise the assignment, and to go in and collect the rents. It is often difficult to put the assignment into operation, however, as the tenants are not inclined to recognize it. Usually it is necessary to resort to the receivership. There is no reason why the owner should not give up possession of the property if he wishes to do so, and instruct the tenants to pay rent to the mort-

gagee. The owner is, however, entitled to an accounting and any surplus must be applied to the amount due to the mortgagee.

15. *Obligation to pay taxes.*—The third covenant made the principal sum due by reason of nonpayment of taxes or assessments. The fifth covenant contains an agreement on the part of the owner to pay such taxes (and also to pay water rates). If they are not paid, this clause gives the holder of the mortgage the right to pay them. The owner then becomes liable for their repayment, and they are added to the lien of mortgage.

16. *Changes in tax laws.*—The sixth covenant has to do with taxation upon mortgages. The loan is made relying upon mortgage tax laws in force at the time, and if any change which affects the mortgage is made in the law the holder has the right to give thirty days' notice requiring the payment of the mortgage. The responsibility for any hardship occasioned to the owner by such procedure rests with the legislative body making the change in the law.

17. *Notices.*—The seventh covenant provides for giving to the owner such notice as the holder of the mortgage may desire to give him. There is no necessity under the instrument for any notice except those the holder may desire to give. Notices are frequently sent, however, notifying the owner of interest becoming due, or fire insurance policies expiring, or taxes and assessments due.

18. *Warranty.*—The eighth covenant includes the

covenant of further assurance and the covenant of warranty, similar to two of the covenants found in the warranty deed. By reason of this covenant any interest in the land acquired by the borrower subsequent to the date of the mortgage, would come immediately under the lien of the mortgage.

19. *Estoppel.*—Under the ninth covenant the owner of the mortgaged premises agrees to sign an estoppel certificate, that is to say, a written instrument which certifies to the amount due on the mortgage. A mortgage is not always a lien for the amount of principal and interest mentioned in it. A payment may have been made by the owner of the property or it may have been modified by agreement. The estoppel certificate is of value to the mortgagee and any assignee relying on it, as it confirms the amount claimed by the mortgagee and estops the owner from claiming any less amount to be due.

Failure to furnish the certificate when requested, within the time specified, may result in the entire mortgage becoming due.

20. *Special agreements in mortgages.*—Besides the covenants described, special provisions, either for the benefit of the owner of the land or the holder of the mortgage may be included in the mortgage. One of these is known as the release clause which states that the holder of the mortgage agrees to release portions of the premises upon payment of a certain sum of money on account of the principal. This provision is of value when the mortgage covers a number of

lots which the owner may sell separately. As he sells one or more lots he pays the mortgagee a specified amount agreed upon, and obtains an instrument releasing the plots sold from the lien of the mortgage.

Another important clause is frequently inserted in mortgages which are junior liens on the property, that is, subject to prior mortgages. This is known as the "lifting clause" and provides that the mortgage is subject and subordinate to the prior mortgage, and shall continue to be subject and subordinate to any new mortgage of like amount and similar terms, made to replace the existing prior mortgage, and that the holder agrees to execute any instrument necessary to effect such subordination.

The subordinate mortgage may further provide that if there is any default in the payment of interest on the prior mortgage, the holder of the junior lien may pay such interest and add it to the amount secured by his mortgage; also, that if any action is commenced to foreclose the prior mortgage, the holder of this mortgage may elect to consider his mortgage immediately due and payable. This provision is valuable to the holder of a mortgage, the lien of which may be jeopardized by default occurring in a prior mortgage, as it helps him to preserve his lien on the property.

21. *Special forms of mortgage.*—There are a number of forms of mortgages which are used as occasion requires. Three of such forms are the following:

(a) Instalment mortgage. The principal feature

of the instalment mortgage is its provision that the principal sum shall be paid in instalments. Sometimes it is provided that certain instalments of principal shall be paid in addition to interest. In other cases it is provided that specified amounts shall be paid, out of which interest on the mortgage shall be taken and the balance of the payment be applied toward the payment of the principal. In the latter case the interest charge becomes smaller as the principal is reduced; hence, as the payment remains the same, the portion applied to principal becomes greater with each succeeding payment.

(b) Building loan mortgages are used to secure advances on a loan made to finance the construction of some improvement on the land. The principal is advanced to the owner from time to time during the progress of the work. The mortgage is made out for the total amount to be loaned, but it is only a lien on the property for the amount actually advanced. As advances are made they are receipted on the bond. In New York, it is necessary to file a building loan agreement in connection with such a mortgage, setting forth among other things, how the advances are to be made.

(c) Trust mortgages are made to a trustee, usually to secure an issue of bonds. Instead of one bond, held by one person, there may be many bonds held by a number of persons, all secured by one mortgage. The mortgage is then made to the trustee who acts for all the bondholders. This form of mortgage con-

tains all the covenants and agreements found in the usual form and, in addition, a number of provisions regarding the rights and duties of the trustee and the individual bondholders. In Canada the form of mortgage or charge depends on whether the Torrens System or Land Titles Act is in force or not. If the property is under the Land Titles Act, the document is usually called a charge, otherwise a mortgage.

22. *Usury laws.*—In many states there is a legal rate of interest and any interest charge above such rate is usury. Economically all usury laws are fallacious, and what is more they fail to protect the borrower. A needy borrower will obtain money on a mortgage and will pay extra interest for the loan in the way of fees and commissions in spite of the usury laws. Extra compensation is paid by borrowers not only to pay for the lender's financial risk, but also on account of the risk the lender takes in breaking the law. If there were no usury laws more money would be attracted to the mortgage market for investment, and the added supply of funds would naturally tend to reduce the rate of interest. Of course, there is usually an ample supply of money for conservative first mortgages, and such loans, as a rule, can be obtained at the legal rate of interest or less.

The State of New York charges a recording tax of one-half of one per cent on mortgages. This tax is usually paid by the borrower, and such payment does not make the mortgage usurious, even tho the mortgage itself bears interest at six per cent, the

legal rate in New York. Payment of the recording tax makes the mortgage exempt from other taxation in the state.

23. *Methods of foreclosing mortgages.—There* are two methods of foreclosure. One is known as a foreclosure by advertisement. It is the more simple but the less used method. It is not an action at law, but merely the execution of the power of sale granted in the mortgage instrument. The law regulates the power to sell by requiring that notice be given to the owner, if he can be found, the posting of notices in public places, and a sale by public auction at a public place. The disadvantage of the method is that it may be difficult to get possession of the property after the sale. Since the rights of the parties have not been passed on by a court, it may be necessary to resort to a long and expensive ejectment proceeding in order to get possession.

The second method of foreclosure is by an action at law. It is an action whereby the rights of the parties are adjudicated by the court, a judgment entered and a sale held under the court's direction. The purchaser at such a sale is entitled to the assistance of the sheriff in obtaining possession, if this is necessary.

The first steps in a legal foreclosure are an inspection of the premises and a search of the records to get the names of all who have or claim to have interests in the property inferior to the mortgage. Such persons are made defendants to the action. A summons and complaint is drawn. A notice of the

impending action (lis pendens) and a copy of the summons and complaint is filed in the County Clerk's office. A copy of the summons and complaint is served on each defendant, and opportunity is given to them to answer. If no answer is put in, a judgment of foreclosure and sale is obtained as a matter of course. If there is an answer, the issue is tried out. The court appoints a referee to compute the amount due and also to sell the property at public auction. The sale is advertised twice a week for three weeks. The referee employs an auctioneer and sells the property to the highest bidder on the day specified. The purchaser usually pays ten per cent of the amount bid at the sale and twenty days later he pays the balance, at which time he gets a deed from the referee and is entitled to possession of the property. The proceeds of the sale are used to pay (1) taxes, assessments and water rates, liens on the property sold; (2) costs of the action, referee's fees and advertising; (3) amount due mortgagee. The balance, if any, is paid into court and is then paid over to those claiming it according to legal priority as if their claims were against the land.

When the property falls into natural divisions, the court may order the parcels to be sold separately and only so much sold as will satisfy the claim of the mortgagee, plus expenses.

REVIEW

What is a bond; a mortgage; a note? State the two legal theories of mortgage. What is the New York law? What is "equity of redemption"?

What are the parties to a bond called, and what covenants do they make? What is the "penal sum"?

How may repayment of the principal sum be made? When and how is interest usually payable?

In case of default in payment, what are the rights of sale? Is the property to be sold as a whole or in separate parcels? When and why may a mortgage debt become due before the agreed date?

Does the mortgage call for the maintenance of the fire insurance? What is the receivership clause? What effect does the mortgage tax law have on the holder?

What are the covenants of further assurance and of warranty; an estoppel certificate; the release clause; the "lifting clause"?

What rights have the holders of subordinate mortgages?

Describe the instalment, a building loan and a trust mortgage. How do usury laws affect borrowers? How may a mortgage be foreclosed without a suit at law? What are the proceedings in a suit?

CHAPTER VIII

TRANSFERS AND CLOSINGS OF TITLE AND TITLE INSURANCE

1. *Growth of modern right of transferring titles.* —Under the feudal system of the Middle Ages, land tenure was a personal relation between the tenant and his overlord, founded upon the necessity of material defense, and carrying with it the obligation on the part of the lord of protecting his tenant and on the part of the tenant of fealty and aid to his lord. The tenant was unable to sever this relationship unless he put in his place some other person selected by and acceptable to his overlord. When he relinquished his holdings he had no voice as to who should take his place. Under such a system commercial transactions with the land were practically impossible. A method of sub-infeudation arose, however, whereby the tenant put in another under him and the under tenant put in tenants under him and so on indefinitely. The evils of this system and the necessity for the freedom of the land led to the enactment of a statute allowing a tenant to sell his holdings and substitute another tenant in his place.

2. *Methods of transferring titles.*—Formerly the transfer of the title to land was effected by trans-

ferring actual possession of the land. Sometimes there was a symbolic act performed, such as breaking a turf from the land and handing it over with words of delivery, such as "I put you in possession of this land." Such a method was crude, often resting upon memory for the validity of the title since no permanent record of the transfer was made. If a man was in possession and he and his ancestors had been in possession as long as anyone could remember, it was necessary to assume that his title was good. This is the foundation of our present title by adverse possession. The system, however, led to many disputes. Men took possession wrongfully, and held possession by force. As the number of transfers increased it was found necessary to enact a statute requiring a written record to be made of every transfer. This was known as the Statute of Frauds. The result of this enactment was that all transactions had to be in writing and later by a deed, the instrument we now use in transferring titles to land.

3. *Instruments used in transferring titles.*—Transfers of land may be absolute, or they may be made as security for an obligation. The instrument usually used to transfer the absolute title to land (or any estate therein) is called a deed or transfer; the instrument used to make the transfer upon security is called a mortgage, or in some cases a deed of trust. Both the deed and mortgage have been considered under separate chapters in this volume of the Text.

Transfers of title may occur by conveyance and

also by operation of law. Transfer by operation of law takes place when a decedent leaves no will. The law then steps in and says who shall get the title. Commercially, we shall consider that all transfers by death, whether they are made by will or not, are transfers by operation of law, while all others are transfers by conveyance.

In the ordinary language of the real estate business, the word "deed" means an instrument used to effect a transfer of the title of real property. Legally, the term includes any formal instrument given under seal. While in New York, and in some other states, it is not necessary that a conveyance of land be under seal, the instrument is nevertheless called a deed. In some jurisdictions under Land Titles Acts it is called a transfer and is not under seal.

The law requires that a deed of land shall be in writing and subscribed. In some states it must be sealed and witnessed. If it is understandable and the subject matter capable of identification, and if it be properly executed, it will transfer the title.

4. *When title passes.*—Title passes only upon delivery of the instrument. Surrender of the instrument to the transferee must be a voluntary act on the part of the vendor. Possession of the instrument obtained by fraud or theft, does not give the transferee the title. From the moment of the delivery all rights of the transferer cease and all rights carried by the instrument to the transferee begin.

Delivery of the instrument must be made by a

person competent in law to make a contract. The grantor must be competent when the instrument is signed, and also when it is delivered. If a man should make a deed to another, retain possession of it and afterward become insane, the deed may be set aside as not having been delivered during the competency of the grantor. In a similar manner, a deed recorded after the death of the grantor may be questioned on the ground that it may not have been delivered before the grantor's death.

5. *Necessity and advantage of recording instruments.*—The execution and delivery of an instrument does not of itself give notice to outsiders that a transfer has taken place. If the transferee takes possession of the property, effectual notice is given, however, as all the world is required, when dealing with the property, to take notice of the rights of the occupant. In cases where the property is vacant, or where the transferee does not become the occupant, some other form of notice must be given. A man might sell his land to one purchaser, deliver a deed and then sell it again to a second person, leaving the two claimants to fight it out. To avoid such contingencies, a system of public records has been devised under which a place for recording conveyances is provided by public authority. The law further provides that the recording of the conveyance on the public records serves as "constructive notice" and sometimes "actual notice" to the world that the transfer has taken place. To be protected, persons dealing with the

property must resort to the records to ascertain the condition of the title, since they are charged by law with a knowledge of everything the records show.

Constructive notice is just as good as actual notice. If A conveys a piece of land to B, and a third party, C, had actual notice of the transfer, a subsequent conveyance by A to C would not be good as against B, and this would hold true whether B recorded his deed or not. But if C had no knowledge of the transfer to B, and if B failed to record his deed, C who purchased the property and recorded his deed before B offered his for record, could hold the title against B. In the second instance, B should have protected himself by promptly recording his deed, as then C would have been charged with constructive notice of the prior transfer, whether he actually looked up the record or not.

To be entitled to a place on the public records, instruments must be acknowledged or proved by a properly qualified officer. The acknowledgment of an instrument is the admission by the grantor to the proper public official that he did execute the instrument for the purposes the instrument is intended to serve. The method of proving the execution of instruments by corporations is described in the chapter on Deeds. Proof of the execution of an instrument by an individual is sometimes made by a subscribing witness. The subscribing witness goes before the official qualified to take acknowledgments, and swears that he is acquainted with the one who executed the instrument,

that he knows him to be the person described in and who executed the instrument, that he was himself present and saw him execute it, and that thereupon, he signed his name as subscribing witness. Such proof is equivalent to a personal acknowledgment and it is used only when a personal acknowledgment cannot be taken.

Officials who are authorized to take acknowledgments are: notaries public, commissioners of deeds, justices of the peace, judges of courts of record, mayors of cities, ambassadors and ministers residing abroad, consuls, vice-consuls, consular agents and commissioners of deeds appointed by the governors of states to take acknowledgments in other states, Masters in Chancery and, in a number of states, Attorneys and Counselors at law or Commissioners for taking affidavits. In order that an instrument which was acknowledged before an official of one state may be recorded in another state, it is usually necessary to add to the acknowledgment, a certificate to the effect that the acknowledging official is authorized to take acknowledgment of instruments intended to be recorded in the state in which he resides, that the certified officer knows his signature, and that the signature is genuine. The certifying officer is the clerk of a court of the county or city in which the acknowledging officer resides or acts.

6. *Transfers of real property by will.*—The person who receives the title to real property by virtue of a will, is known as a devisee. The will is a volun-

tary act of the testator, but the title to the property is carried forward to the devisee at the testator's death by operation of law. A will (except in the case of a soldier on active military service, or a sailor at sea) must be in writing and signed with certain formalities as provided by the statutes of the state or province. Those who take title under wills are not considered purchasers for value, and a deed of the property to a third party executed and delivered during the lifetime of the testator would bar the rights of the devisee in the property. The principle of constructive notice can be invoked only in favor of innocent purchasers or encumbrances for value.

If a person owning real property dies intestate, the property passes to his heirs by operation of law.

7. *Examination of title by inquiry into public records.*—Inquiry into public records should be directed first toward ascertaining the history of the property under consideration, and second toward ascertaining whether any defects in or encumbrances upon the chain of title is disclosed in the history or abstract of title. Such inquiry is necessary since, according to the principle of constructive notice, anyone dealing with the property is charged with a knowledge of the entire contents of the record.

A layman would find so many difficulties in making an examination of title even where public records are kept systematically, that it is usually found necessary to employ an expert for the purpose. Everything affecting the property under examination found

on the record must be noted and an abstract or history of the title made up. With the facts before him, the examiner gives his opinion upon the result. He should be able to state the names of the person or persons in whom the title is vested, and existing defects and encumbrances, if any.

The law of real property is a technical and complicated set of rules. To examine a title one must be to some extent familiar with the principles of law applicable to the subject, must have some degree of experience with the effect of the records and must have the ability to handle and read the indexes to the records.

An attorney who examines a title undertakes to apply his ordinary professional skill in the work, but he cannot guarantee the result. From each link in the chain of title, he must draw conclusions of fact and also of law. For instance, he may trace the title to A, and then find a deed on record from A to B. He is justified in assuming that the record is a copy of an authentic deed, and not of a forgery. Again he may find that B mortgaged the property to C, that C foreclosed the mortgage and that X, as referee in the foreclosure action, deeded the property to D. He must examine the record of the foreclosure and see that it was conducted according to the rules of law. The examiner is justified in his belief in the authenticity of all of the facts shown on record, and if he draws an erroneous conclusion, believing these facts, and using ordinary professional skill, he incurs

no liability to his employer. If a deed turns out to be forged or if some matter which affects the title but which is not apparent from the record, develops later, the employer must bear the loss.

8. *Title insurance.*—Defects in titles often develop years after the examination is made. One may think he has the title and a good right to convey it, when upon a new examination something in the past history is disclosed which shows the title to be defective.

Because of the fallibility of title examiners and of the dangers of defects in titles which are not disclosed or cannot be detected from the public records, the system of title insurance has been devised. Corporations organized for the purpose and authorized by law, undertake to examine and guarantee titles. They use the best professional skill obtainable in doing the work, and they issue a policy of title insurance to the owner or mortgagee, guaranteeing him against loss.

9. *Policy of title insurance.*—The policy issued by a title insurance company usually consists of four parts. The first is the agreement of insurance; the second is a schedule setting forth the details of the subject matter; the third is a schedule of the exceptions or limitations affecting the subject matter; the fourth is a statement of the conditions governing the relations between the company and the policyholder.

Under the agreement of insurance, the company, in consideration of the premium, guarantees to the in-

sured and to his heirs and devisees (not his assigns) that it will insure them against all loss or damage. Their payment for loss, however, shall not exceed the amount which the insured shall actually sustain by reason of any possible defect in the title. The premises are described in the schedule which is annexed to the policy, and any encumbrances or objections are listed.

The amount of insurance is usually the amount the insured paid for the property and this is the maximum that may be recovered. It is often appropriate that the insurance be for more than this amount, especially when the insured intends to add to the cost by expenditures for improvements. The premium paid for the policy is a single premium paid once for all. It is based upon the amount of insurance, and is the same regardless of whether the title was a difficult or an easy one to examine.

10. *Exceptions and limitations upon subject matter of insurance.*—Every exception, encumbrance and limitation affecting the title insured should be clearly set forth in the schedule annexed for the purpose. It is sometimes required, in closing the title, that the insured assent in writing to the items to be included under this schedule. When the policy is issued these items should be carefully examined by the insured, to make sure that they are the ones agreed upon.

Encroachments and other matters shown by a survey will be stated in this section of the policy, and if

no survey has been furnished the policy will state that the company does not insure against such facts that an accurate survey would show.

11. *Conditions of the policy.*—An important clause of the policy provides that the company will defend at its own expense, all actions or proceedings on matters insured against founded on a claim of title or encumbrance prior in date to the policy. Another important condition is that the title is not only good but that it is marketable. All proceedings are conducted and defended by a title insurance company under its direction and at its expense, both as to counsel fees and risk of costs. The insured is indemnified not only against actual loss but is saved from the annoyance incidental to litigation.

A policy of title insurance, unless it is issued to a mortgagee is not transferable. The agreement stipulates that the insured shall be indemnified against loss. If he parts with his property and receives satisfactory compensation for it, the company's guarantee of marketability has been performed. If the insured conveys the property by a warranty deed, and is afterward called upon to make good his warranty for a defect in the title, he can then obtain indemnity from the title company. The policy always protects the insured, but it is unreasonable to expect that it should be transferable.

When a mortgage is assigned, all securities and collateral go with it, and for that reason a mortgage title policy is transferable upon the assent of the company.

In the event of loss, the title company has the option of either paying the loss or taking over the property. If the loss is total and cannot be salvaged (as in the case of a forged deed) the company will pay the loss to the amount of its insurance. Very often time and skill will clear up a defective title. If the company sees a chance of recovery by clearing up the title, it will take over the property, paying the insured its full market value which may be much more than the amount of the insurance.

Whenever a company settles a claim, it acquires every right which the policyholder has against persons who are liable to him by reason of the loss. If a company is held because a mortgage or tax has not been paid, and the insured has a full convenant and warranty deed, the company after paying the policyholder his loss, is entitled to sue the man who made the full convenant and warranty deed so that it may recoup the loss.

The policy of title insurance expressly provides that the insurance does not cover "defects and encumbrances arising after the date of the policy." Everything that happens after that date is in the control of the policyholder.

12. *Use of title policy.*—A title policy should be produced whenever the insured property is being sold or any agreement about it is being made. Care should be taken to make the contract or agreement with respect to the title exactly as it is insured, so that if there is any defect in title or marketability, the

insured can fall back on the insurer. In order to be certain that this detail is observed, it is advisable to have the title insurance company prepare the contract or agreement. The policy of title insurance necessarily stipulates that any untrue statement made by the applicant or policyholder leading the insurer to issue a policy will vitiate it.

13. *Closing the title.*—The ordinary contract of sale or exchange provides for payment of the purchase price and delivery of the deed at a date shortly following. We will assume that in the interim the title has been searched for the purchaser.

Two things are necessary to close a title intelligently: first, a copy of the agreement covering the transaction, and second, accurate information concerning the present status of the title. A study of the first will give an understanding of the bargain and will show what each party is entitled to receive at the closing. The information on the present status of the title is furnished by the attorney or the title company that has examined the title, and will show whether or not it is possible to adapt the title to the proposed transaction.

14. *Report of title.*—When a title is examined by a title insurance company it is advisable to obtain a written report of the title. This is usually furnished in the form of a letter, sometimes in the form of a certificate, and sets forth in whom title is found vested and also all liens, defects, encumbrances and exceptions affecting the title. Sometimes the pur-

chaser's attorneys will have the title examined and reported by a title company, and he will then proceed to close the title himself. It is usual, however, to have the title closed by the attorney in the employ of the title company. The search of the title should be brought down to the very day of closing.

If the title to be conveyed under the contract is one in fee simple, a proper deed conveying such an estate should be obtained at the closing from the owner of the property and all necessary parties should join in the deed. The person to whom the title is conveyed should see also that the title is subject only to those encumbrances which are set forth in the contract, and that if there are other encumbrances, they are disposed of in such a manner that they can be cleared from the record. The same principles apply when a life estate or any other estate is to be conveyed. If it is a mortgage transaction the mortgagee should see that the proper parties join in the mortgage and that on advancing his money, he obtains such a lien on the property as he may desire.

15. *Encumbrances subject to which the purchaser takes title.*—Encumbrances found by an examination of title are of two classes, those subject to which the purchaser is to take the title, and those which must be removed. Contracts of sale frequently provide that title shall be delivered subject to the lien of one or more mortgages, to restrictive convenants and to tenancies of various kinds.

Anyone taking title subject to a mortgage, should

see that the amount, expiration, date, rate of interest and any special clauses are as stated in the contract. If the record differs from the facts claimed by the seller, the purchaser is entitled to have evidence of the change in such form as can be recorded. If the record does not disclose certain facts concerning the mortgage, the purchaser is entitled to a reasonable opportunity to ascertain whether the mortgage is as represented in the contract.

All leasings or lettings affecting the property should be examined to see if they conform to the contract. The purchaser or his representative should not be satisfied with the lease presented to him by the seller at the closing. If possible he should go to the property and find out the claims of each occupant as to his rights in the property. It is advisable also to be on the lookout for agreements for the renewal of leases, rebates of rent, etc.

Restrictive convenants should be read carefully to see that they are the ones mentioned in the contract. Other restrictions frequently are disclosed by the examination, and if they are considered not to affect the value of the property injuriously or to interfere with its intended use, they may be waived by the purchaser. The purchaser's representative should not waive any such restrictions unless the matter has been submitted to his principal.

16. *Encumbrances to be removed.*—After being satisfied as to the encumbrances which are to remain, attention may be given to those which are to be re-

moved. It is the seller's business to have the title clear and to have all instruments necessary to clear it present at the time of closing. It is customary, however, for the purchaser to waive his rights in this respect if it can be ascertained definitely that the encumbrances can be easily removed. For example, if the property appears to be subject to unpaid taxes, it is the duty of the seller to present receipted bills showing payment. It is a very wise precaution to have a certificate from a proper tax authority showing what if any taxes are in arrears. If they are actually unpaid at the time of closing, the seller can leave with the purchaser or his attorney (frequently the title company's representative) sufficient funds to cover the amount of the taxes with accrued interest. Again, the property may be subject to the lien of a mortgage or judgment. In many cases the purchaser can satisfy himself that a satisfaction-piece is at a known place ready to be delivered upon payment of a certain amount of money. The title is closed, the required amount held out, and the purchaser or his attorney obtains the satisfaction piece with the money held for the purpose. It is always desirable in closing a title to exercise every reasonable precaution to protect one's own interests or the interests of the client represented.

17. *Adjustments made at closing.*—The adjustments at closing are made in the form of a debit and credit account. The first debit is the gross amount of the purchase price, which we shall assume to be

$25,000. The next debit relates to the unexpired portion of the fire insurance policies covering the buildings on the premises. This adjustment is made on the basis of the premiums on the policies, prorated over the term for which they were written. If, for example, the closing is on June 15 and the policies were dated October 15 of the previous year, and the premiums totaled $36 for three years, we would figure that eight months had expired and that two years and four months were unexpired. The proportion of the premiums to be charged to the purchaser would therefore be $28. If there is an adjournment of the closing the purchaser sometimes is charged with interest on the balance of the purchase price for the adjourned period. This is done when the closing is made as of the original date, and, unless otherwise stipulated, the interest is at the legal rate.

The purchaser's first credit is the amount paid when the contract was made. Assume in this case the amount so paid to be $1,000. The next credit is the amount of the mortgage subject to which the purchaser takes the property. This mortgage we will assume to be $15,000 with interest at five per cent payable January 1 and July 1. The purchaser is entitled to receive as a credit the interest accrued on the mortgage from the last interest day, January 1. Since the closing is on June 15, interest for five months and fourteen days amounting to $341.67 has accrued.

If the contract provides for a purchase money mortgage in addition to a mortgage already on the property, the amount of that mortgage, which we will consider to be $3,000, would be the next credit.

The purchaser is also to be credited with a proportionate part of the rents collected for the current month. Rents paid in advance on the first of the month would be equally divided, the seller retaining one-half and allowing the purchaser one-half. Rents paid from dates other than the first would be apportioned so that the purchaser will receive the part covering the period subsequent to the closing date. In order to complete our figures, we will assume that the amount agreed as due to the purchaser to cover the adjustment of rent, is $125. Rents due and unpaid are not adjusted at the closing. Either the purchaser or the seller must collect them (as agreed upon at the closing), one making the collections and sending the other party his share.

18. *Other payments made at closing.*—The report of title may show other unpaid obligations—taxes, assessments or water rates. It is not usual to apportion these items unless the contract provides specifically for such apportionment. The total amount of these items, with interest, is often deducted from the money due the seller and turned over to the closing attorney for payment. In the following statement a deduction of $385 is made from the amount due the seller to cover the amounts we will assume he must pay.

In addition to the amount due to the seller, the purchaser must pay the expenses incidental to preparing the purchase money bond and mortgage, recording the mortgage and the mortgage tax. These expenses as shown by our statement total $23.

19. *Closing statement.*—From the foregoing figures, the following statement can be made:

Dr.		*Cr.*	
Purchase price	$25,000.00	Paid on contract	$ 1,000.00
Insurance premiums	28.00	Subj. to mtge.	15,000.00
		Int. 5 Mo. 14 days	341.67
		Purchase money mtge.	3,000.00
		Adjustment of rents	125.00
Total	$25,028.00	Total	$19,466.67
Amount on Cr. side	19,466.67		
Gross balance due seller			$ 5,561.33
Payments to be made by Seller			
Taxes	$350.00		
Assessments	25.00		
Water rates	10.00		385.00
Net balance due seller			$ 5,176.33
Payments to be made by Purchaser			
Drawing bond and mortgage	$5.00		
Recording mortgage	3.00		
Mortgage tax	15.00		
			23.00

In order to carry thru the transaction, the purchaser must provide $5,561.33, and must pay in addition the seller's attorney expenses amounting to $23. Out of the $5,461.33 the seller must pay $385, leaving a net balance of $5,176.33 to be taken away by him.

20. *Closing exchanges, leaseholds and loans.*—The closing statement for exchange transactions contains a double set of debit and credit items. One party is charged with the purchase price of the property to be transferred to him, and credited with the price of the property he conveys to the other party. Mortgages and adjustments are set up in a similar manner. Each party is charged with items he must allow to the other party and credited with those he is entitled to receive. Sometimes the difference in the respective values as stated in the contract, is charged to the proper party instead of showing the values of each parcel and the mortgages affecting each. If there is no difference in the values to be paid by one to the other, the adjustment pro and con are the only items to be considered.

Leaseholds are closed by adjustments of rents between the parties, including the ground rent paid or to be paid to the owner of the land, and the rents paid by the sub-tenants to the lessee. In closing mortgage loans, all items of expense are paid by the borrower, the lender simply advancing the amount of the loan. The closing attorney must see that the mortgage instrument is in proper form and that the report of title shows that the mortgage creates a lien on the premises of the kind contemplated.

21. *Methods of figuring interest.*—In real estate transactions, it is customary to figure interest on the basis of a 360-day year. Each month is considered to be one-twelfth of a year and for the purpose of

short figuring it is customary to take each day as the thirtieth of a month, so as to use the ordinary six per cent method of calculating interest. As a matter of law, in calculations of interest for a period consisting of months and days, each month is considered to be one-twelfth of a year, and only the odd days are figured on the basis of a 365-day year. When figuring interest, it is customary to exclude the first and include the last day.

22. *Rejection of title.*—If a purchaser has good reason for rejecting the title, he is entitled to have returned to him any sum which he has paid on the contract, together with interest at the legal rate from the time when he made the payment up to the time when it was returned to him. He is entitled also to have returned to him his reasonable expenses for examination of title, which means that a person can merely charge the actual cost of examining title in accordance with the customary rate. He cannot obtain consequential damage or compensation for loss of prospective profit, or brokerage paid for bringing about the contract, or loss incurred upon a prospective resale of the property, unless the seller is convicted of fraud in making the contract. Only in case of fraud can the purchaser get secondary damage.

23. *Necessity for accurate survey of the property.*—When a parcel of land is the subject of any commercial transaction, it is important that an accurate survey of it be obtained. The surveyor employed for the purpose makes his return in the form of a dia-

gram, showing the outline and dimensions of the property, the location of every structure upon it, and the extent of any encroachments upon it by adjoining structures. Occasions have arisen where no survey was obtained before closing, which showed that the buildings said to be on the land conveyed were on other land. Only a survey can usually show this.

24. *Encroachments shown by survey.*—Having in mind the extent of the ownership of the person whose land has been surveyed, the survey is examined to see if the structures upon it are entirely within the bounds of the land. If not, there may be a question as to the marketability of the title. If the buildings encroach upon adjoining land, the owner of that land may be able to compel their removal, or may require damages for the encroachment. The buildings may encroach upon the street and the public authorities may compel their removal. The question of marketability can be solved only by a person familiar with the principles of law applicable to the situation.

In considering the effect of encroachments upon the land by buildings erected on adjoining property, the question to be decided is more one of business than of law. The encroachment does not affect the title to the remainder of the land. The question is, has the encroachment diminished the size of the plot so that it is materially different in value from the plot which was the subject of the negotiation? The courts will not compel the purchaser to take a plot materially different from the one contracted for.

Under some circumstances an allowance for the difference in value may be given if the purchaser takes the plot.

A survey should be examined in connection with any restrictions affecting the property. The building may violate some restriction such as one requiring it to be set back from the building line of the street. Party walls, beam rights, etc., should be indicated by the survey. It is often necessary to show old roads and changes in the lines of streets upon the survey.

25. *Survey for building operations and land developments.*—Whenever a building is to be erected upon a lot, a surveyor should be employed to mark the lot lines and to indicate where the structure is to be placed. The surveyor should also be called in from time to time to test the work of the builder in order to guard against encroachments. In connection with a building operation, the survey is also useful in showing grade of curb, sewer levels, etc.

The surveyor is employed when a tract of land is to be laid out in streets and divided into separate lots. The streets are definitely located, blocks are cut into subdivisions and maps are made showing such contemplated changes.

REVIEW

A executes a deed to B and leaves it on his desk. Later B comes in, picks up the deed and goes away with it. Has title passed? Why?

X makes a mortgage to Y, who does not record it. Subsequently he makes a second mortgage to Z and this is placed on

record. Jones, knowing of Y's mortgage, buys the property from X. What are Y's rights?

X makes a will, leaving his homestead to Y. Z, knowing of the will, buys the property during the lifetime of X. What are the positions of Y and Z upon the death of X?

When title to a property where the title has been insured, proves defective, what courses may the title company pursue?

In your state, if a person dies intestate, to whom does the real property descend?

A sells a farm to B, who enters into possession but does not record his deed. Later A, who is dishonest, offers the property to C. C knows B is on the farm but supposes him to be a tenant of A. C buys the farm. What are the rights of B and C?

If you were purchasing a tract of land and the seller executed the deed in another state, what facts would you wish to know? How would you show them?

CHAPTER IX

LEASES

1. *Landlord and tenant.*—A landlord is an owner of an estate in real property, or of an interest therein, when considered with relation to another hiring the property and agreeing to pay rent, who is known as the "tenant."

2. *Definition of rent.*—Rent is a definite periodical return for the use of land. The expression "definite" does not mean necessarily that which is ascertained by the agreement itself, but that which can be made definite. If the return from a farm is to be a share of the produce, while neither party knows in advance what that share will be worth, the fact that the share can be ascertained when the return is to be made, make it a definite return. Hence "leasing on shares" establishes the relation of landlord and tenant.

The return must be periodical as well as definite. A period must be specified when the return is payable. Sometimes it is all payable at one time, as at the beginning or the end of the term. Very often the rent is paid in instalments, either monthly, quarterly, or yearly.

3. *Term of lease.*—The time during which occu-

pancy is to last is known as the term of the lease, or technically as "the term." There is no limit as to what the term may be. It may be one day, one month, one year, or 999 years.

In New York State long-term leases usually are made for twenty-one years with the privilege of one or more renewals for similar terms. The reason for this is that the rent on leases for more than twenty-one years is taxable as personal property to the person entitled to receive it. If the person is not within the state, it may be taxed against the tenant. This tax is an added burden since it is imposed in addition to the ordinary tax upon the land, and to avoid it the expedient of the shorter term with renewal privilege has been adopted.

4. *Assignment of lease.*—The landlord's interest in the rent, his right to receive rent, and his expectation of being restored to possession of the property at the expiration of the term, remains real property. A deed to the property carries with it the right to receive the rent. The tenant's interest, regardless of the length of the lease is personal property, is assignable as personal property and goes to the personal representative rather than to the heirs. Unless the lease expressly provides against it the tenant's rights may be assigned or mortgaged. Any such mortgage would be a lien on the tenant's term or right of occupancy. If a lease provides that it shall not be assigned by the tenant, as leases usually do, and if notwithstanding the covenant, the tenant

assigns the lease, and the landlord knowing of the assignment accepts rent from the assignee, that provision of the lease will be deemed to have been waived. Thereafter the lease is freely assignable. To guard against this possibility, the lease should provide not only that the tenant shall not assign but also that no subsequent assignee shall assign.

An assignment of a lease does not relieve the tenant of liability to pay the rent he has agreed to pay. He is bound on his covenant to pay rent, but is entitled to be credited with any amount collected by the landlord from the assignee. Any occupant other than the original tenant can be held liable for the payment of a fair rental and can be sued for the value of the occupancy during his actual use. He cannot be held for the rent called for by the lease unless an agreement to pay that rent can be shown.

5. *Leases created orally and by writing.*—A lease for the term of one year or less may be created orally. A lease for a term exceeding one year must be in writing and must be signed by the person to be charged. These terms may vary in different states. In New Jersey, for instance, a lease must be for a ten-year-term period, in order to be recorded, and leases may be made orally for any term up to five years. The statute law of the individual states should be consulted when exact information is required. The element of signing and the necessity for expressing clearly the entire contract in the instrument are the same as in the other instruments we

have considered. Some leases may be recorded (in New York those for three years or longer) but they usually are binding upon the parties even tho not recorded. It should be noted that actual notice by occupancy applies to leaseholds as well as to other interests in the land. Possession of the property gives to those dealing with the property actual notice of the tenant's rights. It is not safe to conclude that if a tenant has not recorded his lease the term of it is only a short one.

6. *Monthly tenancies.*—The shortest lease known commercially and to the law is the tenancy from month to month. This is an agreement, oral or written, whereby the tenant hires and the landlord lets the premises for a period of one month only. A term of leasing from week to week comes under this same classification. While the tenancy apparently terminates at the end of the month, it is actually a self-renewing month-to-month arrangement. The tenant usually remains in possession and the landlord receives the rent month after month.

It is a uniform rule, except in New York State, that a notice to quit shall be coincident with the length of the tenancy period. So a tenant from month to month must be given one month's notice, a tenant from week to week, one week's notice ending with the tenant's week, and so on. In New York City, by statute, only five days' notice is required. The requirement of notice to end leases of this kind is reciprocal. This is the common law rule, but an

apparent exception exists in New York State, where a dictum of the court implies that the tenant need not give notice. If the tenant stays over his monthly term for even one day he is liable for another month's rent.

7. *Tenancy-at-will.*—The tenancy-at-will is the longest term of letting in the eyes of the law. The term is indefinite—there is no limit to its duration. The usual arrangement is that a letting is agreed upon, with rent payable monthly, but no *term* is stated. The tenancy-at-will is apt to be confused with a monthly tenancy. If the parties desire a monthly tenancy it should be so provided in the written agreement if there be one, or the rent receipt should read to that effect.

A tenancy-at-will can be terminated by either party at will. In New York City, by statute, all tenancies-at-will end on May 1 of each year and the tenant can remove or the landlord require possession without notice.

8. *Tenancy for years.*—A tenancy other than that from month to month, or at will, is usually for a year or more. The term is fixed definitely by agreement. Such a tenancy ends of its own force, without notice, on the last day of the term. If the tenant continues in possession at the end of the term, the landlord may exercise one of three options. He may dispossess the tenant and obtain possession; he may consider the tenant a hold-over from month to month, or he may consider the tenant a hold-over for a further

period of one year. If nothing be said on either side, the presumption is that of the hold-over on an annual basis and upon the same terms as the former lease.

9. *Ground lease.*—There is a form of lease for years which is sometimes called a ground lease. The feature of this form of lease is that it is a lease of the ground only, the tenant erecting the structure on the land. The term of the lease must, of necessity, be long, in order to induce the tenant to erect a suitable building. There may be one long term, or there may be a term of say twenty-one years with a privilege of one or more renewals for like terms.

The rent fixed by a ground lease is often based on a percentage of the value of the land. In case of renewal privileges, it may be provided that the rent for the renewed term be made a certain percentage of the value of the land at the time the new term commences. The new value is arrived at frequently by arbitration. Usually all taxes, assessments and water rates must be paid by the tenant, so that the return to the landlord is net.

The problem of the tenant is to put a building on the plot and obtain such rents from sub-tenants occupying it as will pay the following charges:

(a) The ground rent.

(b) Taxes and water rates (and assessments if any).

(c) Fire insurance, labor, heat, light and power, repairs, and all expenses incidental to the upkeep and maintenance of the building.

(d) Interest on the amount invested in erecting the building.

(e) An amount sufficient to amortize the cost of the building by the end of the term of the lease, or the end of the last renewal of the lease.

(f) A sum over and above all the foregoing charges to compensate him for his own services and the risk he assumes in undertaking the enterprise.

In some cases it is provided in the lease that at its expiration the landlord shall pay the tenant a fixed sum for the buildings erected. In this case the tenant would only have to amortize the difference between the cost of the building and the sum to be received from the landlord on the surrender of the premises. It should be remembered that the buildings are real estate and belong to the landlord as owner of the fee as soon as erected, but nevertheless the landlord can agree to pay the tenant for them on the expiration of the lease. The maxim is "He who owns the soil owns from the center of the earth to the sky," but but there are many qualifications of this.

10. *Termination of leases.*—Every lease ends at the expiration of its term. Prior to the end of the term leases may be terminated by a voluntary offer of surrender on the part of the tenant and an acceptance of the offer by the landlord. The tenant is liable for rent up to the time of surrender, and thereafter all obligations of the parties cease. Surrender and acceptance may be implied by the acts of the parties. For example, the tenant may vacate the premises and

the landlord may enter and take possession. The re-entry by the landlord may be for the purpose of protecting the property, and yet it may be construed as an acceptance of a surrender. For the protection of the landlord the lease should provide that if the premises become vacant he may resume possession for the account of the tenant, and that the tenant shall remain liable for the rent until the end of the term.

The lease may be terminated and the relation of landlord and tenant severed by a breach in the covenants or conditions of the lease. The conditions may be divided into two classes, those for which the landlord can dispossess the tenant by a summary proceeding, and those for which he cannot dispossess. A tenant can be dispossessed for any one of three causes.

First:—Holding over after expiration of term.

Second:—Non-payment of rent, or for non-payment of taxes and other charges, if the tenant has agreed to pay such charges.

Third:—Unlawful use of the premises.

For the breach of any other covenants of the lease, the landlord is not entitled to dispossess a tenant summarily but to obtain possession he must sue the tenant in a lengthy and expensive ejectment action. Leases can be drawn in a manner that will avoid this, however.

For example, the tenant may covenant to make certain repairs. A provision can be made that if he fails to do so the landlord may make and charge the

cost to the tenant as additional rent, payable with the next instalment. Failure to pay the charge then gives the landlord the right to dispossess the tenant. It may be provided also that if there is a breach by the tenant in other covenants, the landlord may elect to terminate the lease. After such a breach and notice-to-quit the landlord may proceed against the tenant as against the hold-over. All conditions that can be settled by the payment of money may be put in such form that the amount is made as a charge of additional rent; and all other conditions can be made conditional limitations in the term of the lease. The ordinary short-term lease is drawn in simple language, however, and complicated clauses of the kind mentioned are used only in long-term leases of valuable property.

11. *Dispossess proceedings.*—Dispossess proceedings are brought in courts of minor jurisdiction. They are usually commenced by a petition to the court by the landlord setting forth the tenancy and the failure of the tenant to pay the rent and asking for a dispossess warrant. The tenant is served and given an opportunity to appear in court and answer. Judgment is nearly always in favor of the landlord and the warrant is issued. If the tenant fails to move, a public official physically removes the tenant and his belongings from the premises. The warrant is sometimes stayed by the court for a short time, as a matter of compassion.

In some states there is a law allowing the tenant to

pay up the back rent after dispossession and to redeem the premises, providing the lease has a certain number of years to run. Long-term leases usually contain a clause whereby the tenant expressly waives the right of redemption. The dispossess then terminates the lease absolutely. In certain provinces of Canada somewhat similar proceedings are taken. A demand of possession is first served on the tenant, and if he refuses to comply, an application is then made to a judge who appoints a time to determine whether the person complained of was tenant for a term or period which has expired, or been determined, and whether the tenant holds against the right of the landlord and wrongfully refuses to go out of possession, having no right to continue. Evidence is then taken and the matter decided summarily.

12. *Obligations of landlord and tenant.*—The obligation of a landlord is to secure the tenant in possession of the property he has leased, and to protect him in that possession. The obligation of the tenant is reciprocal. He must protect his landlord's interests and give him prompt notice of all matters of which he learns by reason of his occupancy which affect that interest. He may not recognize any person as landlord or pay rent to any person who claims hostility to the maker of his lease. The tenant must be loyal to his landlord and is liable for damages if he breaks that obligation.

Unless there is an express covenant in the lease, there is no obligation on the part of the landlord to

make repairs. Repairs frequently are made by landlords as a matter of expediency and in order to retain their tenants, but usually landlords cannot be compelled to make them. Unless otherwise agreed the tenant does not have to make any permanent repairs, but he must commit no waste upon the premises. He can let the premises go along in ordinary wear-and-tear until they are worn out so long as he does not commit actual waste.

If by reason of some act or omission of the landlord, the tenant is not accorded the occupancy of the premises, or if the premises are not kept so that they can be used for the purpose for which they were hired, there may be a constructive eviction of the tenant which would release him from his obligation to the landlord. Such would be the case where the tenant hired a steam-heated apartment and no heat was supplied. The apartment could not be used for living purposes and the tenant could move. He must take advantage of the landlord's failure at the actual time it occurs, however. In the instance given, if heat were supplied later, the tenant could not then move and allege the former unsatisfactory condition as an excuse.

In some states a lease terminates if there is a fire on the premises which renders it untenantable. If there is no such law, or if there is a provision to the contrary in the lease, the tenant remains liable notwithstanding the fire. If he has the option to remove, he

must do so promptly, or his liability on the lease remains.

REVIEW

A leases a house from B. During the year repairs become necessary. B refuses to make them and A prepares to move. Discuss the rights of the parties.

In the instance given above, suppose A, who is wealthy, assigned his lease to C, who has no property. C refuses to pay rent. What are the rights and liabilities as between A and B?

In your state, what leases must be in writing? What ones must be recorded?

A tenant leases a store for one year. At the expiration of the term he continues in possession, paying rent monthly as usual. After six months he gives notice of intent to terminate his tenancy. What sort of a tenancy has he? What is the landlord's position?

In your state, what are the ways in which a tenant may be dispossessed? What is the procedure?

Who owns a house erected by the tenant under a ground-lease? What are the tenant's problems under this form of lease?

CHAPTER X

BROKERAGE

1. *Broker and his duties.*—"Real estate brokers are those who negotiate between the buyer and seller of real property, either finding a purchaser for one desirous to sell, or vice versa; they also manage estates, lease or let property, collect rents, and negotiate loans on bonds and mortgages." [1] A broker has also been described as "one who makes a bargain for another and receives a commission for so doing." [2]

The broker is an agent or middleman; those he represents are called the principals and they include buyer and seller, lender and borrower, lessor and lessee.

The compensation paid a broker for his services is called commission. It is a certain rate per cent computed on the gross amount involved in the transaction. On sales it is based on the sales price, on exchanges on the values in exchange, on loans on the amount of the loan and on rentals on the rent called for by the lease. Brokers really make their living by doing piece work, as they are paid for each transaction separately. They do not receive a salary. If they did they would not be brokers but salesmen.

A successful broker possesses the qualities of a good

[1] 4 Am. & Eng. Ency. of Law (2nd Ed.), 962.
[2] Potts vs. Turner, 6 Bing. 702, 706.

salesman. He has a thoro knowledge of the thing he is selling and is able to bring it before the right customer in the right way. He has also certain rights and duties of a legal nature. In this chapter we shall consider him briefly as a business man and also outline the most important of the legal principles involved in his activities.

2. *Nature of the broker's business.*—The ordinary real estate broker does a general real estate business. He will earn a commission whenever he can whether by securing a tenant for a cheap flat or by bringing about a sale of property involving thousands of dollars. Many brokers are specialists and will devote their energies only to some particular part of the business. Some brokers work entirely on sales of real estate, others make a specialty of securing mortgage loans while others seek to effect commercial leases. Whether the broker's business is a general one or whether he specializes in some particular part of it, the requirements for success are the same.

The confidence and good-will of his customers are the broker's chief stock in trade. If he obtains the confidence of a customer, that customer will be glad to do business with him again and will recommend him to his friends. In that way the circle of the broker's acquaintance will gradually widen—he will slowly but steadily build up a clientele, and if the uniform experience of these business friends with him is satisfactory, and they find him dependable and truthful,

his business is bound to grow. The underlying principles of success, whether ethical or practical, are the same in this business as in any other business or in any of the professions.

The real estate man should possess a thoro and accurate knowledge of the property he wishes to sell or rent. He should have a diagram showing the exact location, dimensions and shape of the land. He should know all about the buildings on the land—the size, number of floors and number of rooms and the material of which it is built. He should know the age of the building, the improvements it contains, whether it is in good or poor repair, the tenures under which it is held, the rent paid by each tenant, the length of the term of rental and the number of vacant apartments or stores. The foregoing has to do with the physical condition of the building and its present rents and tenants. In addition, information about the mortgages on the property should be obtained—their amount, rate of interest, when due, privileges of prepayment, and the name of the mortgagee.

A convenient way of keeping a record of the properties listed with the broker is by means of a card index or loose-leaf book. The card or sheet should have a printed or typewritten outline to be filled in with the information noted about each piece of property.

Of course, the broker must note in his records the price an owner is asking for property he wishes to sell. The broker's knowledge should tell him whether this price is fair and reasonable or not. Such knowl-

edge is acquired only by experience in making sales himself and by keeping careful notes of sales made by other people whenever this information is obtainable. The broker ought to know if sales of similar property in the same neighborhood have been made and the prices obtained at such sales. He should be able to form an opinion as to the present market value of the property, its value as indicated by the rents it produces and also the possibility of its increasing its value, due to changes in the neighborhood, sidewalks, sewers, water, gas, projected transit lines, increased rents, etc.

Many owners list their property with the broker with the idea of having him find them a purchaser. If a person seeking to buy property comes to the broker, the broker goes over his list with the prospective purchaser, makes a note of what probably will suit the person best and shows these properties to him and then tries to close him on one of them. Sometimes the broker has nothing in his books to suit the buyer. Then he looks around and tries to find something. He may try for months before he finds the property the buyer wants. Again, a salable piece of property may come to the attention of the broker and he will endeavor to find a buyer for it. Often he is successful and makes a good commission. Frequently he does a great deal of work from which nothing comes. While an important transaction brought about pays the broker well, the business is full of disappointments. Impressions may be made, trans-

actions *almost* consummated and then the whole thing may fall thru. The experienced broker has learned to take these disappointments as part of the business, and at once starts in again to work on some other proposition.

A broker should find out that the one offering property is in reality the owner or his authorized representative and also that the owner is able to sell. If he owns the property in a fiduciary capacity, he may not be able to sell it or he may have to obtain an order of the court in order to do so. Sometimes property is affected by restrictions that destroy its usefulness for certain purposes. If the broker knows about such things in advance he may avoid wasting time and energy working up a deal only to find that it cannot be carried out.

3. *Employment of the broker.*—It is a clearly established principle of law that a broker must have been employed by the principal in order to be able to recover a commission for bringing about a transaction. This employment must be either expressed or implied. In order to found a legal claim for commission on a sale, there must be not only a causal but also a contractual relation between the introduction of a purchaser and the ultimate transaction of sale. The usual thing is for the owner to come to the broker and place his property in the broker's hands for sale. At that time the broker should make sure that the owner will pay him the usual commission if he procures a buyer. If the owner agrees to

this, we have a definite and express employment. It would make it even a little better for the broker if the price and terms of sale of the property, together with an agreement to pay commission, were written out and signed by the owner. But the mere fact that the owner voluntarily lists the property with the broker, either by word of mouth or in writing, even tho payment of commission is not mentioned, will be construed in most jurisdictions as an employment of the broker by the owner and will subject the owner to the payment of a commission if the broker sells the property for him.

4. *Volunteers not paid.*—If one approaches the owner inquiring the price of a piece of property, and the terms upon which the owner will sell, and afterward brings a customer to buy the property on the owner's terms, the owner has not become liable for a commission. The inquirer will be considered a mere volunteer and as such not entitled to compensation. Probably in most cases of this kind if the owner were asked in advance if he would pay a commission if a sale were made he would have agreed to do so. Brokers have frequently carried negotiations up to a successful termination, only to wake up to the fact, after the deal was made, that the owner had never employed them. See 70 App. Div. 45 (N. Y.); 4 E. D. Smith 354 (N. Y.).

5. *Employment, implied or by ratification.*—Employment of the broker may be implied from past relations of the parties or from special circumstances. If the broker has been accustomed to sell property

for an owner and has received commissions for doing so, the owner could not refuse to pay him a commission for selling another parcel on the plea that he had not been employed. The past custom of the owner would justify the agent in expecting a commission for the service rendered unless the owner had deliberately said in advance that he would not pay one. Also, if an owner negotiated with one he knew to be a professional broker and whom he knew expected pay for his services he could be held for a commission if the sale were made. The employment of the broker would be implied. Any act of an owner recognizing a claim for commission, such as offering a less amount, raises the presumption of an implied agreement to pay. Employment may be by ratification but only where there is a plain intent to ratify. Thus, if one not previously employed brings the owner a purchaser, and the owner avails himself of the broker's services and continues negotiations thru him, the circumstances indicating in some way that the broker expected to be paid for his services, an implied promise to pay the broker would be presumed. Questions of fact in these cases may be very difficult to determine. It has been well said, however, that an owner cannot be enticed into paying a commission against his will, so the intent to ratify must be very clearly shown.

The Supreme Court of Canada held that the agent who was the effluent cause of the sale was entitled to his commission altho the purchase was on altered terms and by associates of the person to whom the agent in-

troduced the subject. Stratton vs. Vachon 44 S.C.R. 395 (1911).

6. *Employment to sell need not be in writing.*—Written authority of the owner to sell his property is not required now in the State of New York. Chapter 128 of the Laws of 1901 which provides that the broker's authority must be in writing was subsequently declared unconstitutional, and furthermore was repealed by Chapter 516, Laws of 1906, and again repealed by the Penal Law of 1909. In New Jersey and a few other states the written authority is required.

7. *Earning commission.*—The question as to what efforts of the broker entitle him to a commission naturally arises. The answer to this has been made clear by numerous judicial decisions. He must produce a purchaser ready, willing and able to buy the property upon the terms specified by the owner or terms acceptable to him, or he must be the procuring or efficient cause of the sale being made. When the broker is employed to sell the property, he should, as we have already pointed out, obtain full particulars of the property including the price asked by the owner, and the terms on which he will sell. If the owner has stated no terms the broker's customer must offer terms which the owner will accept. In either event if the broker brings a customer who will buy on the owner's terms, the broker has fulfilled his agency and is entitled to compensation. Furthermore, if the broker brings a customer who altho not willing to purchase

on the owner's terms, yet offers other terms which the owner accepts, the broker is entitled to the commission.

The broker is not paid for interesting a prospective purchaser in the property, for making impressions, or for any efforts that are unsuccessful (Sibbald vs. Bethlehem Iron Co., 83 N. Y., 383). He is not entitled to a commission if he abandons negotiations after commencing them, or if the purchaser refuses to deal thru him. This is true in some jurisdictions even tho the sale is made afterward by the owner direct or thru the efforts of another broker. If the owner or purchaser, in bad faith, get together behind the broker's back and make the deal, the broker would be considered the procuring or efficient cause and would be entitled to commission. It is not necessary that the broker guarantee the solvency of his customer. If the customer were of notorious financial irresponsibility the owner could refuse to treat with him, but if he accepts him he cannot claim this as sufficient ground for refusing to pay the broker's commission. If no contract were made the broker suing for commission would have to prove that his customer was able financially to carry out the contract, had one been made. In some cases the purchaser would have to be one who was personally acceptable to the owner, as, for instance, where there are large terms of credit involved, or where a loan is to be made in connection with the sale to a builder improving the land.

It is not necessary that the contract of sale be reduced to writing and signed, altho the signing of a contract is the best evidence a broker has that his customer is ready and willing to purchase. The customer must be one, however, who could execute a binding contract at the time if required to do so. The owner cannot conscientiously refuse to deal with the proposed purchaser, and if he should do so, and the broker could prove that the purchaser was one ready, willing and able to buy on the owner's terms, the owner would be liable to the broker for his commission. The owner would also be liable for commission, if he could not carry out the transaction after a regularly employed broker produced such a purchaser. A case of this kind was one where the seller's wife refused to consent to the arrangements. 33 Misc. 793 (N. Y.).

When the broker advertises a piece of property and a purchaser is attracted to the property and opens negotiations thru the broker, the broker is the procuring cause and is entitled to commission if a sale is made directly between owner and purchaser.

The parties must agree about all of the terms of the proposed transaction. There must be a meeting of the minds. Where the owner has not expressed himself already, all the terms offered must be satisfactory to him. A case is on record where the broker's purchaser required a warranty deed and the owner refused to give one. In this case the form of deed had not been agreed upon. A similar case came to

the writer's attention in which negotiations for the sale of property were practically completed, the price and amount of cash payment having been agreed upon, when the question was raised as to which side should pay the expense of procuring certain mortgages to be placed on the property. Both the purchaser and the seller refused to pay these expenses and the deal fell thru. The minds of the parties never met, and the broker did not earn a commission.

8. *Double employment.*—The broker's duty to his principal is that of any employe to his employer—loyalty, faithfulness and honesty. He is an agent, and as such must do all in his power to serve his employer's best interests. He cannot represent both buyer and seller faithfully and therefore must not accept pay from both, unless each knew that the other was paying a commission. By accepting, or agreeing to accept pay from the opposite side in a transaction, he forfeits the right to receive a commission from his employer. It is a breach of his contract of agency, and a fraud on his principal. Of course, a double employment might be known and consented to by one or both of the principals, in which event it could not be offered by one to whom it was known as an excuse for refusing to pay the broker. The rule against double employment is in accordance with both legal and moral principles—"No man can serve two masters." It applies whenever the agent has been intrusted with the slightest discretion. Where the broker merely acts as a middleman to bring the principals together,

the price and terms being arranged entirely between them, he can be the agent for both sides. In such cases the broker has no discretion whatever, and if employed by both principals he can receive commission from both.

9. *Secret profits.*—A broker employed by an owner to sell property cannot become the purchaser unless the owner clearly and unmistakably assents to it. In the New York case of Clark against Bird, reported in 66 Appellate Division 284, a broker was intrusted with property to sell for the owner. He received offers, but advised that they be declined. Finally he told the owner that one Jones would purchase the property for $10,000 and advised acceptance of the offer. A contract was drawn and signed between the owner and Jones at $10,000 but at the closing of the title the deed was taken in the broker's name. The owner claimed that she was cheated as she supposed Jones to be the real purchaser. Her action to rescind the sale resulted in the deed being set aside. The court in this case, quoting from Story on Agency said, "An agent employed to sell cannot himself become the purchaser; and an agent employed to buy cannot himself be the seller. So an agent employed to purchase cannot purchase for himself." A broker cannot get the owner to fix a net price for his property and then effect a sale at a greater price and keep the difference. He would be liable to the owner for the secret profit so realized. In Bain vs. Brown, 56 N. Y., 285, a broker brought about a sale for an owner

at $17,000. Before title closed he made a contract in his own name with another party for the same property at $26,000. He took an assignment of the first contract and then directed the owner to deed direct to the second purchaser, not disclosing to the owner the price under the second contract. The Court of Appeals held that the owner was entitled to the benefits of the advance upon the second sale.

The foregoing does not mean of course that one not acting as agent for the owner could not get a net price from the owner and then sell at a larger price and make the profit, nor does it mean that the terms of employment may not allow the broker to make as a commission all he can realize over and above a certain price. This must be expressly stated in the contract of agency, however. The agent cannot take a secret profit.

10. *Broker's authority.*—The broker may not sign a contract of sale for an owner unless authorized to do so. The ordinary employment of the broker does not include his authority to execute a binding contract of sale in the owner's behalf. In the states of New York and New Jersey and some others, if authority to sign a contract has been given to the broker, such authority need not be in writing.

If a broker employs another broker to sell property the latter must look to the first broker for commission. No privity of contract exists between the second broker and the owner. The owner can expressly authorize the broker to employ sub-agents and in such

cases he would be directly liable to the sub-agents for their commission. The owner might also ratify the employment of the sub-agent and thus become liable to him for commissions.

11. *Disclosing information.*—The broker is bound to reveal to his employer all information he may have affecting his employer's interests in the property. Withholding information which naturally could be expected to influence the conduct of the employer in dealing with the property is a fraud on the part of the broker. He forfeits his right to recover commission by such an action. The broker, however, does not have to violate confidences. If a purchaser negotiate confidentially with a broker for some property and wishes the transaction made in the name of a dummy, the broker does not have to reveal to the owner the real purchaser. He should tell the owner, however, that the purchaser is a dummy acting for an undisclosed principal.

12. *Statements made by broker.*—A broker can make statements regarding the property based upon information furnished by the owner which he believes to be true. If a purchaser relies upon these statements and contracts to purchase the property, but later rescinds upon learning that the statements were untrue, he will be relieved of his contract and is entitled to receive his money back. The broker, however, in such a case is entitled to his commission. He was not at fault.

If the broker makes unauthorized misrepresenta-

tions, a purchaser who had been induced to contract by reason of such misrepresentations would be entitled to receive his money back and be relieved of his contract. Under such circumstances the broker would not be entitled to commission, because of his fraud. If the owner accepts the fruit of the broker's work and enters into a contract with the purchaser knowing of the misstatements of the broker, he will be liable to the broker for a commission, even tho the purchaser be subsequently relieved of his contract. In a case of this kind the owner is deemed to have ratified the broker's acts.

It is an established rule of law that a principal is bound by the acts of his agent when the agent acts within the scope of his apparent authority. By reason of this an innocent purchaser is relieved of his contract not only when it has been induced by misrepresentations made by the owner directly, but also when made by the broker employed by the owner. The broker can recover commission on the sale, however, whenever the misrepresentations were made by authority of his employer or were ratified by the employer. When the misstatements were unauthorized and the employer innocent, the broker loses his right to compensation.

Misrepresentations sufficient to relieve one from a contract must be about some material fact such as the amount of the rents, the size of the plot or the price actually paid for the property by a former buyer. Mere opinions as to present or future value will not be

considered as misrepresentations even tho exaggerated. The New York courts have also decided that an unintentional misrepresentation on the part of the owner did not amount to a warranty to the broker and did not authorize a recovery of commission when the purchaser refused to enter into a contract. The misrepresentation concerned the size of the plot. It was held that the broker was employed to sell the plot, with which he was familiar, and not a certain number of feet of land. (Hausman vs. Herdtfelder, 81 App. Div. 46.)

If the broker makes misstatements to his employer to induce him to enter into a contract of sale, it is a breach of the broker's duty of good faith and a fraud upon his employer, and will cause a forfeiture of the broker's right for commission. This is so even tho the employer carry out the contract.

13. *Termination of agency.*—Where no time for the continuance of the contract is fixed by its terms, either party is at liberty to terminate it at will, subject only to the ordinary requirements of good faith. Usually the broker is entitled to a fair and reasonable opportunity to perform his obligation, subject of course to the right of the seller to sell independently. But that having been granted him, the right of the principal to terminate his authority is absolute and unrestricted, except only that he may not do it in bad faith and as a mere device to escape the payment of the broker's commission. The right of the parties to terminate the agency is clearly established by judicial

decisions. The agency is also terminated by the death of either principal or agent; by the destruction of the subject matter; by the bankruptcy of the principal; by mutual consent and by the sale of the subject matter by other means than thru the agent. It is of course terminated when the object of the employment is performed, and it can generally be considered terminated after the lapse of a reasonable length of time, except that the principal must act in good faith in considering it terminated for this cause.

14. *When commissions are due.*—It can be laid down as a rule that commissions are due and payable as soon as the broker has done the work for which he was employed; that is, as soon as he has brought to the owner a purchaser ready, willing and able to buy on the owner's terms. The broker does not have to wait until title closes or even until the contract is signed. This may be modified, however, by express agreement made prior to the time the commission is earned. If, after he has earned his commission, an agreement is made by the broker to wait until title closes, or to make his commission dependent upon the happening of any event or to take less than the usual commission, or to waive commission entirely, it is not binding upon the broker and can be disaffirmed by him. It cannot be enforced against the broker because no consideration was given for his promise. There are cases, however, where the owner in closing negotiations with a purchaser either agrees to accept a lower price for his property, or modifies the terms of

the financial settlement upon the express condition that the broker waive his right to commission until a later date, or accept a smaller amount. Such an agreement is for a consideration and is binding.

The broker is not responsible for failure of the customer to complete the contract. If the broker brings a customer answering the description we have already noticed, and the owner enters into a contract with him, it is the owner's responsibility to get a sufficient sum paid on the contract as earnest money at least to cover the broker's commission. If the owner does not do so, that is his affair. He may accept a fifty dollar deposit upon the sale of a piece of property and become liable to the broker for a one hundred dollar commission. The broker does not lose his commission because the owner fails to require a large enough deposit on the contract.

When the payment of commission is deferred until passing of title by valid agreement, and title never passes because it is defective, or for any other reason for which the seller is responsible, the broker is entitled to commission notwithstanding such agreement.

15. *Purchaser sometimes employer of broker.*— The broker is usually employed by the owner to sell the owners' property. As the agent of the owner his duty is toward his employer. In the final analysis, however, the purchaser pays the commission, for it can be assumed that the owner includes the commission in determining the price of his real estate. In a few cases the purchaser employes the broker to buy prop-

erty for him, and then the broker's duty is toward the purchaser. All that has been said about the agent's duty to his employer applies with the same force when the purchaser is the employer. Furthermore, it is considered perfectly proper for a broker employed by a purchaser to go to an owner and get his lowest price and obtain an agreement from the owner that out of the price the broker shall get a commission. The owner in such cases knows he is dealing with an agent for the purchaser, and the purchaser knows the owner pays the broker a commission. Brokers assembling large plots for buyers frequently have made this arrangement. The site for the terminal of the Pennsylvania Railroad in New York is an example. In some cases the owner is asked to quote his lowest net price, the commission being paid by the purchaser.

16. *Rate of commission.*—Rates of commission are fixed by custom and agreement. There is no legal fixed rate of commissions, but the customary rate in the community will be understood to be the rate unless there is an express agreement for a different one. It is poor business for brokers to accept less than the customary rate. A short, interesting and instructive article, and collection of authorities applicable to the laws in Canada relating to commissions to real estate agents may be found in Volume 48, Canada Law Journal, page 549.

REVIEW

What is necessary to entitle a broker to compensation for his services?

In your state is it necessary for an agreement for the sale of land to be in writing?

When is the broker's commission due?

A broker brings purchaser and seller together. They then pass title between them and the broker's claim for commission is refused. What are the broker's rights?

Make a list of the things you would wish to know about a property someone brought for you to offer for sale.

How would you set about finding a market for the property?

What are the reciprocal rights and duties of principal and broker?

If either party fails to complete a transaction, is the broker responsible?

INDEX